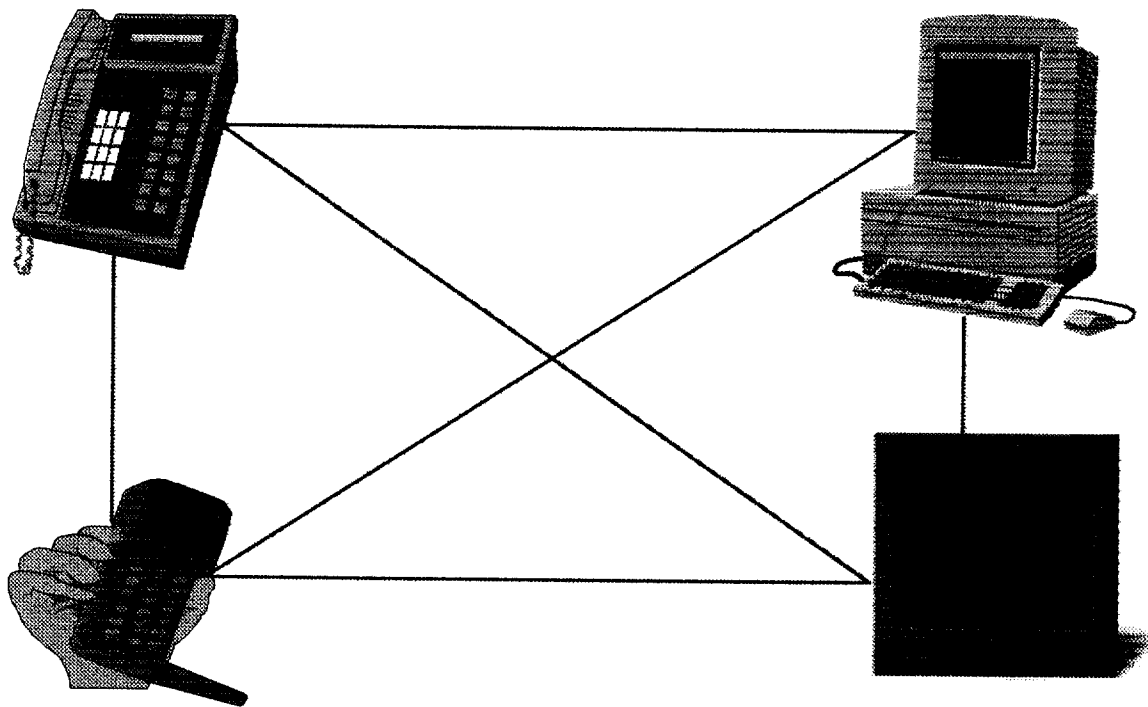


Report to the Tennessee General Assembly

THE STATUS OF LOCAL TELECOMMUNICATIONS COMPETITION IN TENNESSEE

1997-1998



MARCH 1999

THE STATUS OF LOCAL TELECOMMUNICATIONS COMPETITION IN TENNESSEE

1999 Report of the Tennessee Regulatory Authority to the Tennessee General Assembly

TABLE OF CONTENTS

<u>Section</u>	<u>Page</u>
I. Executive Summary.....	iv
II. Introduction.....	1
III. Compliance of Market Participants with Public Chapter 408.....	4
A. Certification of Telecommunications Service Providers.....	4
B. The Status of Local Telephone Competition in Tennessee.....	12
C. Significant TRA Decisions.....	15
D. Price Regulation.....	22
E. Small and Minority-Owned Telecommunications Business Assistance Program.....	28
IV. The Status of Universal Service in Tennessee.....	35
V. Availability of Telecommunications Services and Technological Changes in the Marketplace.....	39
A. Service Availability and “The Last Mile”.....	39
B. Technological Changes.....	41
VI. Federal Telecommunications Initiatives.....	47
VII. Compatibility Between Providers.....	51
VIII. Service Performance of Providers.....	53
IX. Telephone Assistance Programs.....	64
X. Appendices.....	66

APPENDICES

Section

- Appendix A: Chapter 408 of the Public Acts of 1995
- Appendix B: BellSouth Telecommunications Price Regulation Order
- Appendix C: Statistical Data on Incumbent Local Exchange Companies
- Appendix D: Service Areas of Incumbent Local Exchange Carriers
- Appendix E: Tennessee Local Resellers
- Appendix F: Tennessee Long Distance Resellers
- Appendix G: Tennessee Cellular and PCS Providers
- Appendix H: Tennessee Cable Television Providers
- Appendix I: Tennessee Internet Access Providers
- Appendix J: TRA Order on Challenge to Small Company Exemption

TABLES

<u>Section</u>	<u>Page</u>
Table 1 TRA Activity in 1998	xiii
Table 2 Local Telecommunications Providers, 1995-1998	3
Table 3 Types of Local Telephone Competition	5
Table 4 Breakdown of Telephone Access Lines	6
Table 5 CLEC Activity by Location	8
Table 6 Facilities-Based Competition	9
Table 7 Incumbent Local Exchange Companies (1998 Access Lines) .	10
Table 8 Companies Certificated in Tennessee to offer "Facilities-Based" Local Telephone Service (CLECs)	11
Table 9 Status of Local Competition	14
Table 10 Price Regulation	23
Table 11 Significant TRA Decisions Since the Passage of the Tennessee Telecommunications Act of 1995	26
Table 12 Telephone Subscribership in Tennessee (1990)	38
Table 13 "The Last Mile"	40
Table 14 The Federal Telecommunications Act of 1996	50
Table 15 Telecommunications Consumer Complaint Trend	54
Table 16 Percent Change of Consumer Complaints by Industry	54
Table 17 Trend of Slamming Complaints	56
Table 18 Geographical Analysis of Telephone Complaints	58
Table 19 Local Telephone Company Complaint Types	59
Table 20 BellSouth Complaint Analysis	61

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EXECUTIVE SUMMARY

In 1995, the Tennessee General Assembly revised the laws for regulating telecommunications in Tennessee. A year later Congress re-wrote the Federal telecommunications laws in the first major rewrite of Federal telecommunications laws since 1934. Both the State and Federal acts introduced competition in local telephone markets, called for reduced regulation, and directed the preservation of universal telephone service. While the new laws establish the basic framework for achieving these goals, state and federal regulators, like the TRA, must adopt rules and policies to implement this framework.

This is the Tennessee Regulatory Authority's (TRA) second report to the Tennessee General Assembly on the status of local telephone competition in Tennessee. The report provides details on TRA actions since the implementation of the 1995 Telecommunications Act. Included are statistics on Competitive Local Exchange Carriers (CLECs) and incumbent local exchange companies, as well as details on significant decisions by the TRA and the impact of those decisions on the development of local telephone competition in Tennessee.

Competitive Activity

For the first time since the passage of the 1995 Act, there is small but measurable activity by facilities-based competitive providers in Tennessee. As of September 30, 1998, fifteen (15) facilities-based competitors were offering local service to approximately 65,265 lines in Tennessee, primarily to business customers in the State's four (4) largest metropolitan areas. This represents 2% of the total lines open to competition or about 7% of the business lines open to competition. These companies have invested \$170 million in

equipment and facilities in Tennessee since 1995. In contrast, on December 31, 1996 only six (6) facilities-based competitors were offering local telephone service in Tennessee, serving 300 lines. In 1996, competitors had invested \$56 million in equipment and facilities. Twenty-three (23) resellers are also providing local service to 27,914 lines, 1% of the lines open to competition. The majority of those lines are residential. Very little competitive resale activity is taking place in rural areas. The TRA currently has eleven (11) local telephone applications pending approval by the TRA.

The nation's three (3) largest long distance providers, AT&T, MCI/WorldCom and Sprint, are certificated to provide local telecommunications in Tennessee, as are numerous other national local providers such as NextLink, TCG, Intermedia and e.spire. At this time, however, the participation of these three (3) long distance companies in local telecommunications is limited. Also, the TRA's recent certification of the Chattanooga Electric Power Board represents the first electric municipality certificated to provide local telephone service in Tennessee. Chattanooga anticipates that it will begin offering telephone services before the end of 1999. Also of significance is the recent approval of Ben Lomand Communications as a CLEC to provide telephone service in Warren and White counties. Ben Lomand Communications is an affiliate of Ben Lomand Telephone Cooperative. This is the first application by a telephone cooperative or its affiliate to compete in the local telephone market.

The Status of Competition

The development of competition for local telephone services in Tennessee has been slowed by a number of factors. First, local telephone service requires more facilities and more capital than long distance telephone service. Long distance networks reflect a \$55 billion investment spanning 100,000 miles nationwide. The local telephone network represents a \$300 billion investment covering 4,000,000 miles. Also, the lack of activity by the nation's largest cable television providers has caused competition to evolve slower than many had anticipated. In 1995, the nation's largest cable providers were actively developing business plans to enter the local telecommunications markets. However, by

end of 1996, the cable providers had all but abandoned their telecommunications plans and their present involvement in telecommunications is limited.

Competition has also been delayed by legal challenges to the telecommunications acts, or to regulatory actions taken under the acts. TRA decisions on telephone directories, directory assistance, classification of services, reciprocal compensation, the small company exemption from competition and arbitration decisions have all been appealed and are pending in various courts. FCC decisions on interconnection, unbundled network elements, universal service and advanced services have also been appealed. The FCC's rules on interconnection and competition were overturned by the Eighth Circuit Court of Appeals but recently reinstated, in part, by the United States Supreme Court. This is a landmark decision that establishes the ground rules for interconnection with the Bell Operating Companies and should have a great impact on the development of local telephone competition in the nation.

One of the ways BellSouth has responded to the impending local telephone competition is by offering special pricing arrangements to selected customers. These arrangements, offered to large and medium-sized business customers, provide discounted prices to customers who commit to continue using BellSouth's service for a specified period of time, typically two to four years. BellSouth has offered 175 contract service arrangements since 1995, raising concerns over the potential impact of these contracts on the development of a competitive marketplace. A docket has been opened by the TRA to study the impact of these contract service arrangements.

Slower than expected technological developments have also delayed the progress of local telephone competition. Today, most facilities-based providers in Tennessee are providing local telephone service using a combination of their own facilities and the facilities of the incumbent providers. For example, competitors may purchase their own switching equipment but rent loops (lines) from the incumbent local provider. The Federal Telecom Act of 1996 requires the Bell Operating Companies to "unbundle" their networks so that new providers can purchase network elements from the incumbent providers.

Because it is not economically feasible to duplicate the local loop from the telephone switch to the customer's premise, competing providers are currently leasing local loops from the incumbent provider, its biggest competitor.¹ Competing providers are investing billions of dollars to advance technologies such as wireless and coaxial cable to compete with the "last mile" of the incumbents. AT&T, NextLink, Teligent and even Microsoft have made significant investments in alternative loop technologies. Until economically viable alternatives to the incumbents' "last mile" are developed and working, most industry experts contend that local telephone competition will not be able to flourish.

The billions of dollars being invested in local telecommunications technologies is a positive sign that local telephone competition will emerge. Also, a number of electric municipalities in Tennessee, like the Chattanooga Power Board, appear to be "gearing up" to enter the telecommunications markets, another positive sign. The role that electric companies will play in the evolution of local competition is unclear at this time, but their embedded facilities and customer base suggest that electric companies will have a definite impact on the emergence of local telecommunications competition.

TRA Decisions and Pending Proceedings

The role of telecommunications regulators has changed dramatically with the passage of the acts. Implementation of the new laws has proven to be an arduous task. Previously, the primary responsibility of the state's telecommunications regulators was to set prices based on financial forecasts. Today, the primary focus of regulators is the implementation of the new laws to bring fair local telephone competition to the state of Tennessee and to mediate disputes between competitors. Virtually every decision made by the TRA considers state laws, federal laws, court decisions and the public interest.

Nineteen ninety-eight was the busiest year of the TRA's brief existence. The TRA issued 314 orders, established 193 utility dockets, held hearings on 75 days and mediated 2,653 complaints, all exceeding the previous totals of the TRA's predecessor, the Public

¹ This local loop is commonly referred to as the "last mile" to the customer's premises.

Service Commission. In addition, the TRA investigated 430 tariff filings, reviewed 69 interconnection and resale agreements and reviewed the applications of 161 resellers and payphone providers.

It is the mission of the TRA to facilitate the development of fair competition in Tennessee by balancing the interests of consumers and telecommunications providers. In the past two years, the TRA has made decisions on wholesale discounts to competitors, competitors' presence on telephone directories, "slamming" and "cramming," unbundled network elements and universal service; all of which are critical to achieving this mission. Also, the educational discounts on telephone services required by the TRA have played a vital role in providing Internet hook-ups to the state's schools and libraries.

For multiple providers of telephone services to exist, there must be compatibility between providers so that customers of the different providers may call each other. Both the State and Federal telecommunications acts require all providers of telecommunications to interconnect their facilities with the facilities of other carriers. As of December 31, 1998, the TRA has approved twenty (20) interconnection agreements between competing carriers, four (4) of which were arbitrated by the TRA in accordance with the federal act.

One of the most significant TRA decisions concerned the small telephone companies' exemption from competition. The Tennessee Act protects incumbent telephone companies with less than 100,000 lines from local telephone competition unless the incumbent elects to compete outside of its service area. In February 1998, Hyperion of Tennessee, a competing provider, challenged that exemption by requesting permission from the Authority to compete for customers in the area served by Tennessee Telephone Company. Hyperion argued that the small company exemption constitutes a "barrier to entry" in violation of the federal act. Hyperion relied upon the Federal Communications Commission's (FCC) recent preemption of similar laws in Texas and Wyoming. The TRA found, however, that the small company exemption was essential to preserve universal service and is consistent with the federal act. Hyperion's appeal of this decision is now pending before the FCC.

The 1995 Tennessee Telecommunications Act also allows incumbent telephone companies to choose a new form of regulation, price regulation, for setting the prices of its telephone services. This allows incumbents to set prices based on aggregate revenues instead of a forecast of earnings as is done in traditional regulation. Under price regulation, rates are set by the company subject to a cap on the revenues. The rates, however, cannot be discriminatory or anti-competitive.

The Federal Telecommunications Act allows the regional Bell Operating Companies (BOCs) to enter the interLATA long distance market once their networks are open to competing providers. Since the divestiture of AT&T and the Bell System in 1984, BellSouth and the other BOCs may only offer long distance within the LATA (local access transport area). For example, BellSouth is permitted to provide long distance service between Nashville and Cookeville (intraLATA) but not Nashville and Memphis (interLATA). Thus far, the FCC has rejected all five (5) applications filed by BOCs to enter the interLATA long distance markets. While no formal application has been filed with the FCC by BellSouth for permission to enter the interLATA long distance market in Tennessee, the TRA does have an ongoing docket currently containing approximately 40,000 pages of evidentiary records to review BellSouth's compliance with the federal act.

Price Regulation

The three (3) largest incumbent local exchange companies in the state, BellSouth, Sprint/United (a.k.a. United Telephone-Southeast) and Citizens, have elected price regulation. Sprint/United and Citizens were approved for price regulation in 1995 and 1996 respectively. BellSouth's application for price regulation was ultimately approved on December 9, 1998 after appeals to the State Court of Appeals and the Tennessee Supreme Court. The Authority's Order in this case can be found in Appendix B. The TRA's latest decision is still subject to further appeal.

Price regulated companies are allowed to increase rates for one service while decreasing rates for another as long as the aggregate revenues are not increased.² The rates for basic services, however, are frozen for four (4) years from approval of the price regulation plan. For example, in 1996 Sprint/United implemented a \$.29 directory assistance charge while reducing switched access charges to long distance companies. After intervention by the Consumer Advocate Division of the Tennessee Attorney General's Office, an extensive hearing was held. The Authority found that the General Assembly did not intend for directory assistance to be construed as a basic service in the statute and that the \$.29 directory assistance charge is permitted as a matter of law. Nevertheless, the TRA increased the monthly free call allowance from the three calls proposed by the company to six calls and exempted disabled persons from directory assistance charges. In addition, persons over 65 years of age were exempted upon request. Appeal of this decision is pending before the Tennessee Court of Appeals.³

Universal Service

Consistent with state and federal statutes, the TRA is addressing universal service in Tennessee. Universal service is the provision of "residential Basic Local Exchange Telephone Service at affordable rates" (T.C.A. § 65-5-207(a)). Encouraging competitors to serve residential customers throughout the state without raising monthly telephone rates

² The price regulation statute classifies incumbent services as basic or non-basic services. Basic services consist of an access line, dial tone, touch-tone and usage. Also included in basic service are Lifeline and Link-Up services, federal subsidy programs, 911 service and educational discounts. All other services are classified as non-basic including custom calling features such as Caller ID and three-way calling, long distance service and operator surcharges. Prices for non-basic services are set as the company deems appropriate subject to the limitations discussed above.

³ In 1997, Sprint/United proposed increases to residential ISDN rates, call forwarding, and operator assisted calls while reducing business ISDN rates and switched access charges to long distance companies. After testimony and hearings on this matter, the Authority denied Sprint/United's adjustment, finding that residential ISDN is a basic service and that rates cannot be increased until the October 15, 1999 pursuant to state statute. Currently, Sprint/United has a filing pending proposing increases to intraLATA long distance rates in the Tri-cities area and northeast Tennessee, and increases to Caller ID and Call Forwarding services. The company is proposing to offset these increases with reductions to the rates for dedicated private lines to business customers and custom calling packages. The Consumer Advocate has intervened in this proceeding but has agreed to allow Sprint/United to place the rates into effect subject to refund if not approved by the TRA. A hearing on this filing is pending.

may require a special fund to subsidize residential telephone service in high cost areas. Tennessee's Telecommunications Act gives the TRA the ability to consider such a fund, while the federal act establishes a national mechanism under the FCC, but allows states to establish their own system as well. Moving in parallel with national proceedings before the FCC, the TRA has an open docket to consider universal service funding for non-rural carriers.

Small and Minority-Owned Telecommunications Businesses

The Tennessee Act also requires telecommunications providers to submit annual plans to the TRA for purchasing goods and services from small and minority-owned telecommunications businesses and for providing technical assistance to such businesses. The act also established a fund to provide for loan guarantees, technical assistance, and consulting and education services for small and minority-owned telecommunications businesses. In 1998, the TRA reviewed 344 plans and collected contributions to the fund. The TRA also conducted a survey to determine the effectiveness of this program. Only eleven (11) companies out of the thirty-nine (39) surveyed indicated that they awarded at least one (1) contract to a small or minority-owned business during 1996 and 1997. Nevertheless, companies such as BellSouth, AT&T, MCI and Sprint/United have well-established programs for soliciting business from small and minority-owned businesses. Small incumbent companies such as Loretto Telephone, Millington Telephone, United Telephone and Ardmore telephone also appear to be making meaningful efforts to contract services to small and minority-owned businesses.

Service Quality

Local telephone companies' complaints have increased by 10% since 1996, long distance companies' by 33% and resellers' by 42%. The most common complaint against long distance companies and resellers is "slamming," the unauthorized switching of a consumer's telephone service provider. Slamming complaints rose from 68 complaints in 1991 to 570 in 1998. In response, the TRA has stepped up its enforcement actions by

issuing several show cause orders against long distance companies. The TRA has also promulgated new rules addressing slamming.

The largest increase in consumer complaints against local telephone companies is delays in the installation of new service. Some of the delays exceed 30 days for new service installations. This complaint category has increased 77% since 1996. The companies are actively working to reduce these delays. For example, BellSouth which had 315 of the 339 complaints in this category, is hiring over 100 new employees to address this and other service related problems in Tennessee. The TRA will continue to closely monitor this complaint category.

Finally, the exhaustion of telephone numbers led to the creation of two (2) new area codes in the past (3) years, 423 in east Tennessee and 931 in middle Tennessee. Consistent with the national trend, it is expected that east and middle Tennessee will need additional area codes in 1999 and 2001, respectively.⁴ While the explosion of services requiring telephone numbers, beepers, wireless and Internet services, has affected the area code situation, inefficient utilization of telephone numbers is the underlying problem of area code exhaustion. Many telecommunications providers reserve large blocks of numbers for future use. The TRA has established a task force to study number exhaustion and submit recommendations on how to better utilize telephone numbers in Tennessee.

⁴ In implementing the 423 and 931 area codes, the TRA concluded that requiring a portion of the affected subscribers to change their area codes was the most feasible and popular alternative.

TRA Activity in 1998

- ◇ Opened 193 Utility Dockets
- ◇ Issued 314 Orders Involving Utility Matters
- ◇ Investigated 430 Utility Tariff Filings
- ◇ Reviewed 69 Interconnection and Resale Agreements
- ◇ Investigated 161 Reseller and Payphone Provider Applications
- ◇ Held Hearings on 75 Days During Year
- ◇ Investigated and Heard 8 Requests for CLEC Certification
- ◇ Mediated 2653 Consumer Complaints
- ◇ Conducted 7 Formal Rule Violation Investigations
- ◇ Collected \$105,000 in Fines for Rule Violations
- ◇ Approved 14 Mergers and/or Stock Acquisitions
- ◇ Promulgated "Slamming and Cramming" Rules

Table 1

II. INTRODUCTION

On June 6, 1995, Governor Sundquist signed the Tennessee General Assembly's Telecommunications Act of 1995 into law. This Act removed the statutory impediments to the entry of competitors into the former monopoly local telephone service areas, allows incumbent telephone companies to choose price regulation, permits special funding to preserve universal service, and created a program to aid small and minority-owned telecommunications businesses. As the law exempted small-company territories from the entry requirements, the areas served by BellSouth and Sprint/United, a Sprint subsidiary, were primarily affected. These two (2) companies serve 85% of the local telephone lines in the state. By the end of 1995, 13 certificates for Competing Local Service Providers had been approved. State law also requires the Tennessee Regulatory Authority (TRA) to produce this report for the General Assembly every two (2) years.

Subsequently, President Clinton signed the Federal Telecommunications Act of 1996 on February 8, 1996. This act seeks to promote competition in telecommunications markets nationwide. It provides for the resale of local telephone company services; for setting the prices local companies charge competitors for connecting to their networks; for preserving universal service as competition develops; and the conditions under which the Bell Operating Companies, such as BellSouth, may provide interstate and intrastate long distance services. It also forbids legal barriers from deterring entry into local telecommunications markets. By early 1997, the Federal Communications Commission (FCC) had promulgated its rules on interconnection pricing, certain aspects of which were appealed to the federal courts. Also, by this time, the Tennessee Regulatory Authority had approved nine (9) interconnection agreements between BellSouth and potential competitors in the local telephone markets.

By the end of 1998, fifteen (15) competitors were offering local service in Tennessee, primarily to business customers in the urban areas. These companies have invested \$170 million in Tennessee since 1995. They serve about 2% of the total lines open to competition or about 7% of the business lines open to competition. In addition,

twenty-three (23) resellers are also providing local service. Although resellers serve only about 1% of the lines open to competition, the majority of those lines are residential. Very little of the competitive activity, however, is taking place in rural areas.

The development of competition in the local telephone market in Tennessee has been slowed by legal challenges to the telecommunications acts, or by regulatory actions implementing the acts, and by slower than expected technological developments. Challenges to the FCC's rules for setting interconnection prices, for example, were appealed through the Appeals courts to the U. S. Supreme Court, while companies in Texas have challenged parts of the federal act directly. A number of decisions by the TRA under the Tennessee act also have been appealed to state courts. Finally, the development and deployment of new cable television and wireless technologies for providing local telephone services have occurred less rapidly than anticipated in 1995-96.

Nevertheless, the acts did prompt rapid growth in activity before the state's regulatory agency. Since 1995, rules for collecting the Small and Minority-Owned Telecommunications Business fund contributions and for the certification of Competing Telecommunications Services Providers were promulgated. Four (4) interconnection agreements between competing carriers were arbitrated under the federal act and 21 have been approved, along with 49 resale agreements. Proceedings on Universal Service and Permanent Prices for Unbundled Network Elements are also in progress before the TRA. Three (3) applications for price regulation were received and acted upon. Thirty (30) certificates for Competing Telecommunications Services Providers have been reviewed and approved, with eleven (11) more pending at the end of January 1999.

The remainder of this report reviews these and other significant occurrences in the development of competition in Tennessee telephone markets. Specifically, the following seven (7) subjects are discussed:

1. Compliance of market participants with Public Chapter 408.
2. Status of universal service in Tennessee.

3. Availability of services and technological changes in the marketplace.
4. Federal telecommunications initiatives.
5. Compatibility between providers.
6. Service performance of providers.
7. Telephone assistance program.

The report also contains appendices on incumbent local exchange companies and their competitors, wireless telecommunications, providers of cable television and Internet access, and local and long-distance resellers.

Local Telecommunications Service Providers

1995-1998

Certified Providers at Year End

<u>Year Ending</u>	<u>CLECs</u>	<u>Local Resellers</u>
12/31/95	12	0
12/31/96	18	6
12/31/97	23	28
12/31/98	30	63

Table 2

III. COMPLIANCE OF MARKET PARTICIPANTS WITH PUBLIC CHAPTER 408

This chapter addresses the major provisions of the Tennessee Telecommunications Act of 1995 and how these provisions have been implemented and enforced by the Tennessee Regulatory Authority. Included in this chapter are sections on certification of competing providers, the status of local competition in Tennessee, significant TRA decisions, price regulation and the Small and Minority-Owned Telecommunications Business Assistance Program.

A. Certification Of Telecommunications Service Providers

T.C.A. §65-4-201 requires all telecommunications service providers to be certificated by the TRA. Since passage of the 1995 Telecommunications Act, 29 certificates have been granted to companies wishing to provide local telecommunications services. Nine (9) of these certificates were granted by the TRA during 1998. This section of the report provides an overview of the types of competitors, and statistics on competing providers in Tennessee including CLEC's (facilities-based providers), resellers, and the incumbent local exchange carriers.

Types of Local Telephone Competition

Three (3) forms of competition exists in Tennessee's local telecommunications market; 1) Resale; 2) Facilities-based and; 3) Combination of resale and facilities-based services. New facilities-based providers are commonly referred to as competitive local exchange carriers, or CLECs.

Under the resale method, competitors purchase an existing service from the incumbent provider and resell the exact service to end-users. Resale is attractive to many providers because it allows providers to enter the market with minimal investment. On the other hand, because of fixed profit margins and the lack of pricing flexibility and service offerings, this is not considered the optimal method of competing and many of the large competitors shy away from resale.

Facilities-based providers (CLECs) build their own networks to provide competitive local exchange telephone service. CLECs typically require a substantial up-front capital investment to provide local service. In addition, CLECs must obtain access to rights-of-way in order to build facilities. However, once the facilities are in place the potential profit margin is greater for CLECs than for resellers. Because of the capital investment required, many CLECs first test the local markets as pure resellers before building their own networks.

In Tennessee, CLECs are providing service either entirely over their own networks or in combination with the networks of the incumbent providers. For example, CLECs may purchase their own switching equipment but rent loop facilities, the wires running from the switching equipment to the consumer, from the incumbent local provider. The Federal Telecom Act requires the Bell Operating Companies to “unbundle” their networks so that new providers can purchase network elements from the incumbent providers.

This “combination” approach has proven to be the most popular approach for new competitors in the local telephone market. This method of competition, however, suffered a setback in July 1997, when the Eighth Circuit Court of Appeals found that the Bell Operating Companies do not have to offer combined network elements to the CLECs. Instead, under the Eighth Circuit’s decision, the CLECs were required to purchase the individual elements and combine the elements themselves.

Types of Local Telephone Competition

- ◇ **Resale** - Competitors purchase a service from the incumbent and resell the exact service to end users.
- ◇ **Facilities-Based** - Competitor uses own facilities to provide competitive service.
- ◇ **Combination** - Competitor uses a portion of own facilities and facilities of incumbent to provide competitive service.

Table 3

However, the Eighth Circuit's decision was recently overturned by the United States Supreme Court and BOCs must now offer network combinations to competitors.

Statistics on Telecommunications Service Providers

As of September 30, 1998, there were 3.4 million telephone access lines in the state. Of these lines, 3.1 million or 91% are served by companies subject to local telephone competition. The remaining 400,000 lines in the state are served by small independent companies and telephone cooperatives who are currently exempt from competition by state statute. Three percent (3%) or 93,000 of the lines subject to competition are served by the competing providers, CLECs or resellers. This percentage is consistent with the national average of competitive local telephone activity.

<u>Breakdown of Telephone Access Lines</u>		
<u>Company</u>	<u>Access Lines</u>	<u>% of Total</u>
<u>Lines Subject to Local Competition</u>		
Incumbent Carriers	2,998,990	88%
Competitive Carriers:		
- Resale Lines	27,914	1%
- Facilities-Based Lines	65,267	2%
<u>Lines Not Subject to Local Competition</u>		
Incumbent Carriers	195,656	5%
Cooperatives	127,262	4%
Total	3,415,089	100%
Data as of October 31, 1998		
<i>Table 4</i>		

Competitive Local Exchange Companies (CLECs)

CLECs, the facilities-based providers, are serving 65,265 lines in the state (as of September 30, 1998). This represents 2% of the total lines subject to local competition and 7% of the total business lines subject to competition. Virtually all of these lines are business lines located in the metropolitan areas of the state. Business customers in metropolitan areas are the lowest cost customers to service because they typically are in densely populated locations close to the telephone company's switching facilities (the central office). Table 5 shows CLEC activity by county.

The TRA has certified thirty (30) CLECs to provide local telephone service in Tennessee. At the end of 1998, fifteen (15) of these companies were actually providing service in Tennessee, having invested \$170 million in Tennessee facilities. This investment equates to 7% of BellSouth's net Tennessee investment. Table 8 includes a list of all the CLECs certified by the TRA since the passage of the state's 1995 Telecommunications Act. NextLink is the most active CLEC in Tennessee, serving more customers and investing more in facilities than any other CLEC in the state. The TRA currently has eleven (11) local telephone applications pending approval.

The nation's three (3) largest long distance providers, AT&T, MCI/WorldCom and Sprint, are certificated to provide local telecommunications in Tennessee. At this time, however, these three (3) companies are not active in Tennessee's local telecommunications market. The TRA's recent certification of the Chattanooga Electric Power Board is significant in that it represents the first Tennessee electric municipality certificated to provide telephone service in Tennessee. Chattanooga Electric Power Board anticipates that it will begin offering telephone services before the end of 1999.

Also of significance is the recent approval of Ben Lomand Communications as a CLEC to provide telephone service in Warren and White counties. Ben Lomand Communications is an affiliate of Ben Lomand Telephone Cooperative. This is the first

application by a telephone cooperative or its affiliate to compete in the local telephone market.

<u>CLEC Activity by Location</u>	
<u>County</u>	<u>% of CLEC Lines</u>
Davidson	39%
Shelby	35%
Knox	19%
Hamilton	6%
Others ^{1/}	2%
	100%

^{1/} Includes Williamson, Rutherford, Sumner, Blount, Montgomery Cheatham, Maury and Wilson As of 10/31/98

Table 5

Resellers

Sixty-three (63) local resellers have also been certified by the TRA. Twenty-three (23) of these companies are currently reselling local services in Tennessee. These twenty-three resellers are serving 27,916 lines (1%) in the state. Local resale is the only area where there is activity in the residential markets. As of September 30, 1998, Resellers were providing service to 17,879 residential lines. CommSouth and Tel-link are the most active local resellers in the state.

Incumbent Local Exchange Companies

Tennessee has twenty-seven (27) incumbent local exchange companies in the state, nine (9) of which are telephone cooperatives. BellSouth is the largest incumbent provider in the state, serving 78% of the total lines. Sprint/United, serving upper east Tennessee, is the second largest incumbent serving 7% of the total lines in the state. Detailed statistical

data on incumbent providers' revenues, access lines and customers can be found in Appendix C.

Competitive Local Exchange Carriers (CLECs)
(Facilities Based Competitive Providers)

- ◇ Thirty CLECs Certified to Operate in Tennessee; Eleven Applications Currently Pending.
- ◇ Fifteen CLECs Currently Offering Local Service in TN.
- ◇ CLECs Serving 2% of the Total lines Available to Competitors.
- ◇ CLECs Serving 7% of the Business Lines Available to Competitors.
- ◇ Virtually all CLEC Customers are Business Customers in Urban Areas.
- ◇ CLECs Have Invested \$170 Million to Provide Telephone Services in Tennessee Since 1995.
- ◇ NextLink is the Most Active CLEC in Tennessee and has Made the Largest Investment.
- ◇ TRA has Approved 20 Interconnection Agreements Between CLECs and Incumbent Providers (four of those agreements arbitrated by the TRA).

Table 6

Since passage of the 1995 Telecommunications Act, BellSouth's access lines have grown an average of 3.9% per year, while local revenues have grown by 6.4% annually. However, as shown in Table 7, the access line and revenue growth in 1998, while still growing, appears to have tapered off in comparison with the three (3) previous years. In fact, since July 1997, BellSouth's business lines as reported to the TRA, have declined by 6,000.

The fact that BellSouth's local revenues are growing more rapidly than its access lines indicates that customers are using more services such as custom calling features (Call Waiting, Caller I.D., Three-Way Calling, etc....). In addition, BellSouth's net investment has remained flat since 1995, suggesting that BellSouth is serving these new customers using its embedded investment without significant additional investment.

Incumbent Telephone Statistics
BellSouth - Tennessee Operations
1995-1998

	<u>Growth Rates</u>^{1/}			
	<u>July</u> <u>1995</u>	<u>July</u> <u>1996</u>	<u>July</u> <u>1997</u>	<u>July</u> <u>1998</u>
Access Lines: Business	7.3%	8.3%	5.8%	-2.2%
Residence	3.5%	3.4%	3.4%	3.6%
Total Revenues (Combined)	4.3%	5.4%	7.5%	2.7%
IntraLATA Revenue	5.5%	8.2%	7.6%	4.6%
Operating Expenses (Combined) ^{2/}	3.9%	0.6%	-7.0%	3.3%
Gross TN Investment	4.9%	3.6%	5.1%	5.2%
Net TN Investment	3.5%	0.9%	0.6%	0.4%

Note: Since July 1997, BellSouth's business lines have declined by 6,000 lines.

^{1/} Represents growth over previous 12 months

^{2/} Excludes depreciation and income taxes

* As reported by BellSouth

Table 7

***Companies Certificated in Tennessee to Offer
"Facilities-Based" Local Telephone Service
(CLECs)***

Approved

AT&T**	e.Spire**	NextLink**
ATS of Tennessee	GTE**	SouthEast
BellSouth BSE	Hyperion**	Sprint
Blue Star	ICG**	TCG**
Brooks Fiber**	Intermedia**	Teligent
BTI	LCI**	Time Warner**
Chattanooga Power Board	Level 3	US LEC**
Citizens	Logix	US West
Comm. Depot	MCI/WorldCom**	WinStar**
DeltaCom	New South**	
Digital Tel.		

Pending

ALEC	Helicon	NA Comm.
Ben Lomand	Hyperion	Network Plus
BellSouth BSE	Interpath	PV Tel
Dakota	Load Point	

****Currently providing local telephone service in Tennessee.**

Table 8

B. The Status Of Local Competition In Tennessee

For the first time since the passage of the 1995 act, there is small but measurable activity by facilities-based competitive providers in Tennessee. At this time, however, there is virtually no activity by facilities-based providers in the rural areas or residential markets. The CLECs appear to be finding market niches to compete with the incumbents. For example, many large telecommunications users are subscribing to CLEC services as a back-up to their incumbent services, providing redundancy in their operations. In addition, certain CLECs are offering only high speed data services and not voice services.

Local telephone competition has not evolved as rapidly as many have forecasted in the three (3) years since the passage of the federal act. However, we must not discount the fact that BellSouth has been a monopoly provider of local telephone services in Tennessee since 1920 and that this transition to a competitive marketplace will take time. Also, local telephone service requires more facilities and more capital than long distance telephone service. While the pace at which competition will evolve is uncertain, the billions of dollars being invested in networks by potential competitors such as AT&T, NextLink, Sprint, Teligent, MCI/WorldCom and Microsoft nationwide is a positive sign. Also, the state's larger municipal electric companies, like the Chattanooga Power Board appear to be "gearing up" to enter the telecommunications markets which is another positive sign. The role that electric companies will play in the evolution of local competition is not clear at this time, but their embedded facility and customer base seems to make for a logical convergence.

The evolution to a competitive market has been slowed by court battles. Many major decisions by state and federal regulators have been appealed. In fact, the large number of decisions on appeal is a major reason that the federal telecom act has not been fully implemented. TRA decisions on telephone directories, directory assistance, price regulation, classification of services, reciprocal compensation, the small company exemption from competition and arbitration decisions have all been appealed and are pending in various courts. FCC decisions on interconnection, unbundled network

elements, universal service and advanced services have also been appealed. The FCC's rules on interconnection and competition were overturned by the Eighth Circuit Court of Appeals but recently reinstated, in part, by the United States Supreme Court. This is a landmark decision that establishes the ground rules for interconnection with the Bell Operating Companies and should have a great impact on the development of local telephone competition in the nation.

One of the ways that BellSouth has responded to the impending local telephone competition is by offering special pricing arrangements to selected customers. These arrangements, offered to large and medium sized business customers, provide discounted prices to customers who commit to continue using BellSouth's service for a specified period of time, typically two to four years. Since 1995, BellSouth has offered 175 contract service arrangements to Tennessee business customers. The TRA has expressed concern over binding these customers to long term contracts and the potential impact on the development of a competition marketplace. A docket has been opened by the TRA to study the impact of these contract service arrangements.*

Status of Local Competition

- ◇ Significant CLEC activity in the urban, business market.
- ◇ Virtually no activity in the rural or residential markets.
- ◇ CLECs are finding market niches:
 - Data services - ADSL
 - Back-up networks
 - Densely populated areas
- ◇ Some major players who are not presently actively marketing local telephone service appear to be “gearing up” for market entry.
 - AT&T
 - MCI/WorldCom
 - Microsoft
 - Sprint
 - Teligent
- ◇ The role of electric companies (including municipals) is not yet known.
- ◇ The Federal Telecom Act has not been fully implemented.
- ◇ The evolution to a competitive market has been slowed by court battles and slower than expected technological advances.

Table 9

C. Significant TRA Decisions

Both the 1995 State Telecom Act and the 1996 Federal Telecom Act introduced competition in local telecommunications markets, called for reduced regulation and required the preservation of universal telephone service. The revised laws lay out the basic framework for achieving these goals. It is the responsibility of state and federal regulators, however, to adopt rules and policies to implement this framework. Needless to say, the role of telecommunications regulators, such as the TRA, has changed dramatically with the enactment of the above legislation. Previously, the primary responsibility of the state's telecommunications regulators was to examine financial forecasts and set prices based on those forecasts. Today, the primary focus of regulators is to implement the provisions of the revised telecommunications acts, to bring fair local telephone competition to the state of Tennessee, and to arbitrate disputes between competitors. Implementation of the new laws has proven to be an arduous task. Virtually every decision made by the TRA requires consideration of state laws, federal laws, court decisions on regulatory matters and the public interest.

It is the mission of the TRA to facilitate the development of fair competition in Tennessee by balancing the interests of consumers and telecommunications providers. This section discusses how the TRA has proceeded to achieve that mission through its decisions of the past two years.

Wholesale Discounts

The Federal Telecom Act requires incumbent local exchange carriers to offer service "to resellers at wholesale rates." On January 17, 1997, the TRA ordered incumbent providers BellSouth and Sprint/United to offer all of their local services to certified resellers at a wholesale discount. This discount is based on the "avoidable costs" of the incumbent provider (i.e., the savings realized by the incumbent provider of not providing the service to the end user). For example, when BellSouth provides service to a reseller, who in turn resells the service to the end users, BellSouth saves on marketing and customer service costs. BellSouth's wholesale discount is 16% if BellSouth provides

operator services such as directory assistance, and 21.5% if the reseller provides its own operator services.

Challenge to Small Company Exemption From Local Competition

Tennessee statute prohibits competitors from entering the local markets of incumbent providers with fewer than 100,000 lines "unless such company voluntarily enters into an interconnection agreement with a competing telecommunications service provider, or unless such incumbent local exchange telephone company applies for a certificate to provide telecommunications services in an area outside its service area existing on June 6, 1995" (T.C.A. §65-4-201(d)). This provision essentially exempts the small telephone companies of the state from local telephone competition unless the small incumbent company elects to compete outside its service area. As a result, only three (3) incumbent companies are subject to local competition: BellSouth, Sprint/United and Citizens Telecom. BellSouth and Sprint/United both serve more than 100,000 lines, while Citizens, with only 96,000 access lines, has elected to compete outside of its incumbent service area thereby forfeiting its exemption. These three (3) companies serve 88% of the access lines in the state.

In February 1998, Hyperion of Tennessee, a competing provider, requested permission from the Authority to serve customers in the incumbent area of Tennessee Telephone Company, an incumbent provider owned by TDS Telecom serving only 60,000 lines in the state. Hyperion argued that the small company exemption constitutes a "barrier to entry" in violation of Section 253 of the federal act and that the FCC preempted similar laws in Texas and Wyoming. The TRA found, however, that the small company exemption was essential to preserve universal service and is consistent with the federal act. This decision was appealed to the FCC where a decision is pending. The Authority's order in this matter can be found on Appendix J.

Competitive Rules

The TRA promulgated rules for local telecommunications providers that became effective on June 15, 1998 (Rule Chapter 1220-4-8). The provisions of these rules cover: 1) application and certification procedures for Competing Telecommunications Services Providers; 2) transfers and abandonments of these certificates; 3) inspection fees; 4) tariff and pricing rules for competing companies; 5) procedures for consumer and anti-competitive complaints, and other violations of state law; and 6) enhanced 911 emergency services.

Unbundled Network Elements

The federal act requires Bell Operating Companies to make their networks available to competitors and to separately price the individual components of their networks so that competitors only have to purchase the portion of the network needed. For example, a competitor may have its own switch and only need to buy the loop from BellSouth. The federal act requires BellSouth to unbundle the switch from the loop.

The TRA has an ongoing docket to establish prices for unbundled network elements. At present, two (2) weeks of hearings have been held on this matter. On June 30, 1998, the Authority ruled on 19 issues involving the cost methodology and assumptions to be used in calculating the cost of the network elements. Additional decisions are forthcoming.

Universal Service Fund

Both the Tennessee Telecommunications Act and the Federal Telecommunications Act call for support mechanisms to preserve universal telephone service. The federal act expands universal service beyond access to traditional telephone service. The federal act also calls for elimination of implicit rate subsidies, and provides financial assistance for Internet access to schools, libraries and health care facilities.

The TRA is currently involved in proceedings to define what universal service includes, how much it will cost to provide and how it will be funded. On March 24, 1998, the TRA issued its first ruling on the creation of an intrastate universal service fund. In that decision, the Authority ruled on 52 issues and sub-issues which define universal service and the parameters for identifying subsidies in existing rates. Additional decisions on universal service including rate re-balancing and access charge reform are forthcoming.

Dialing Parity and Number Portability

The Federal Telecom Act requires all telecommunications carriers to provide its competitors with the same dialing arrangements as it provides its own customers. For example, if BellSouth customers can complete a call dialing seven digits, BellSouth must also configure its facilities so that competitors purchasing service from BellSouth have the ability for its customers to complete that same call by dialing seven digits instead of using an access code (1-800 or 10xxx). The TRA has previously approved dialing parity plans for Citizens and Sprint/United, and on February 8, 1999, BellSouth's dialing parity plan was approved by the TRA for immediate implementation.

The federal act also requires all providers to implement number portability. Number portability allows a customer to change companies without changing telephone numbers. Interim number portability is currently in place and the TRA is working with the industry to establish the priority listing of telephone offices to be upgraded to provide permanent number portability throughout the state.

Telephone Directories

It is the responsibility of the incumbent provider to include directory listings of the customers of competing providers in the telephone directories it publishes. Competing providers have also requested a presence on the cover of the directories. On September 23, 1997, after an evidentiary hearing, the TRA ordered BellSouth to include the names of competing providers on the cover of the white pages directories. This decision was appealed by BellSouth to the State Court of Appeals where a decision is pending.

Subsequent to the Authority's initial ruling on telephone directories, NextLink filed a complaint with the TRA contending that BellSouth would not place its name and logo on the cover of the 1999 Nashville White Pages. BellSouth argued that the TRA's previous decision did not apply to NextLink. On October 15, 1998, the Authority ordered BellSouth to include NextLink's name and logo on the cover of the 1999 Nashville directory. BellSouth has also appealed this decision.

BellSouth Entry Into InterLATA Long Distance Market

The federal act allows the regional Bell Operating Companies (BOCs) to enter the interLATA long distance market once their networks are open to competing providers. Since the divestiture of AT&T and the Bell System in 1984, BellSouth and the other BOCs may only offer long distance within the LATA (local access transport area). For example, BellSouth can provide long distance service between Nashville and Cookeville (intraLATA) but not Nashville and Memphis (interLATA). Thus far, the FCC has rejected all five (5) applications filed by BOCs to enter the interLATA long distance markets. While no formal application has been filed with the FCC by BellSouth for permission to enter the interLATA long distance market in Tennessee, the TRA does have an ongoing docket currently containing approximately 40,000 pages of evidentiary records to review BellSouth's compliance with the federal act.

New Area Codes in Tennessee

Tennessee, like other states, is witnessing an unprecedented demand on area codes. A review of the increase in the nationwide demand for area codes is insightful. In 1991, three (3) new area codes were implemented nationwide, compared to 37 new area codes for 1997. Our state has had to wrestle with implementing two (2) new area codes (423 for East Tennessee and 931 for Middle Tennessee) over the past three (3) years. And relief does not appear to be in sight. It is expected that East and Middle Tennessee will have to have an additional area code during 1999 and 2001, respectively. The FCC has given authority to the TRA to implement area code relief in Tennessee.

While the explosion of new services requiring telephone numbers, beepers, cellular and PCS wireless services and the demand for additional telephone lines to connect to the Internet has affected the area code situation, another important factor in this issue is the advent of new competitive local providers requesting telephone central office codes. The problem of area code exhaustion is not a shortage of telephone numbers, but rather a shortage of telephone central office codes. A central office code is the three (3) digits of a telephone number following the area code and is used to provide, among other things, location routing for calls. Providers request central office codes when they decide to enter a particular market. Each code contains 10,000 individual telephone numbers whether or not the company needs this many numbers. This means that a telecommunications provider can be assigned a code for Nashville and only provide service to 50 customers while tying up an additional 9,950 telephone numbers. Under the present system, no other company can use these 9,950 telephone numbers. This inefficient utilization of telephone numbers is the underlying problem with the area code exhaustion. The TRA has established a task force to study this problem and submit recommendations on how to better utilize central office codes in Tennessee. This report is due during the second quarter of 1999.

The changing of telephone numbers is a lose-lose proposition for consumers. Whenever an area code change takes place, consumers must either change their telephone numbers or dial additional digits to complete local calls. The new competitive paradigm in telecommunications must have a new method of allotting central office codes in order to ensure a smooth transition from the monopoly paradigm.

Administrative Rules

The adoption of administrative rules is one method by which the Tennessee Regulatory Authority implements state law. Put another way, administrative rules puts flesh and blood onto the laws passed by the General Assembly and signed by the governor.

Since 1996, the TRA has either adopted or promulgated three (3) different sets of administrative rules. These rules deal with a wide range of issues from outlining the basic requirements for local telephone competition to regulations designed to prevent the unauthorized switching of a consumer's long distance service provider, sometimes referred to as "slamming."

Slamming and Cramming Rules

The 100th Tennessee General Assembly passed Public Chapter 709 in its second session. This statute addresses the problem of "slamming," the unauthorized changing of a consumer's long distance service provider. This Public Chapter, among other things, doubled the fine to \$100 per day per offense for companies found guilty of slamming and directed the TRA to establish rules and regulations to implement the chapter.

On December 2, 1997, the TRA initiated a rulemaking docket for the purpose of revising its anti-slamming rules. A total of six (6) companies, including the Attorney General's Consumer Advocate Division participated in the hearing. The TRA approved slamming rules on December 17, 1998 and forwarded them to the State Attorney General for review. Additional discussion on slamming is found later in this Report.

Public Chapter 709 also addressed the problem of billing for unauthorized services on a consumer's telephone bill, sometimes referred to as "cramming." This Public Chapter prohibited the placing of charges on a telephone bill without the permission of the consumer and, like the slamming rules, doubled the fine to \$100 per day per offense for companies found guilty of cramming and directed the TRA to establish rules and regulations to implement the chapter.

Educational Discounts

The Authority has issued two (2) rulings over the past two (2) years to assist in providing affordable Internet access to Tennessee's schools and libraries. The TRA's September 18, 1997, order certified to the FCC that Tennessee is providing discounted

telephone services to schools and libraries, thus making all of Tennessee's schools and libraries eligible for federal funding for Internet hook-ups. Then on March 24, 1998, the

TRA issued a finding that allows schools and libraries to receive both federal and state discounts for Internet hookups. This coupled with the intense efforts of the Department of Education ensures that Tennessee's students have access to this valuable learning tool.

D. Price Regulation

The 1995 Tennessee Telecommunications Act permits incumbent telephone companies to choose a new form of regulation called "price regulation" for setting the price of its telephone services. Price regulation allows incumbents to set prices based on aggregate revenues instead of setting prices based on a forecast of the companies earnings and a fair rate of return, as is done with traditional rate of return regulation. Under price regulation, rates are set by the company, unless found to be discriminatory or anti-competitive.

Upon entering price regulation, the statute requires the TRA to conduct an "audit" to determine if the applicant's earnings fall within the range of reasonableness previously established under rate of return regulation. If the earnings fall within this range, then the rates existing on June 6, 1995, become the initial rates on which the price regulation plan is based. If the earnings are above the range, then a contested proceeding is initiated to establish the initial rates for the price regulation plan. If the earnings are below the range, the incumbent telephone company may request the Authority to initiate a contested proceeding. In the contested proceeding, "to determine a fair rate of return on the company's rate base using the actual intrastate operating revenues, expenses, rate base and capital structure as audited by the Authority" (T.C.A. § 65-5-209(c)).

The three (3) largest incumbent local exchange telephone companies in the state, BellSouth, Sprint/United and Citizens have elected price regulation. Sprint/United and Citizens were approved for price regulation in 1995 and 1996 respectively. BellSouth's

price regulation application was ultimately approved on December 9, 1998, after the PSC's original decision was appealed to the State Court of Appeals and the Tennessee Supreme Court.⁵ The TRA's decision has been appealed.

Price Regulation

- ◊ Annual price changes limited by aggregate revenue cap.
- ◊ Cap based on inflation rate in previous year.
- ◊ Only aggregate revenues are regulated.
- ◊ Under rate of return regulation, prices set by regulators after hearing.
- ◊ Under price regulation, prices set by company unless discriminatory, anti-competitive or barred by statute.

Table 10

The price regulation statute classifies the incumbent's services as basic and non-basic services. Basic services consist of an access line, dial tone, touch-tone and usage. Also included in basic service are Lifeline and Link-Up services, federal subsidy programs, 911 service and educational discounts. All other services are classified in the non-basic category. Non-basic services include custom calling features such as Caller ID and three-way calling, long distance service and operator surcharges.

Under price regulation, prices are set by the company. The statute does, however, include restrictions on the price adjustments permitted. For example, the aggregate revenue generated by the prices cannot exceed the aggregate revenue cap, prices for basic services and call waiting cannot be increased for four years from the date the price regulation plan becomes effective. Also, the amount of annual rate increases to basic residential service (after the four-year freeze) and interconnection services are capped under the statute. Other than the aggregate cap, prices for non-basic services are set as the company deems appropriate as long as they are not anti-competitive or discriminatory.

⁵ TRA order included in Appendix B.

As previously indicated, BellSouth was placed under price regulation in 1998 after lengthy court battles. BellSouth's original price regulation application was filed on June 20, 1995 and approved by the Tennessee Public Service Commission on January 23, 1996, after finding that BellSouth's earnings exceed a fair rate of return and requiring BellSouth to reduce its rates by 56.3 million dollars. BellSouth subsequently appealed this decision to the Tennessee Court of Appeals contending that the PSC incorrectly conducted the audit required by T.C.A. § 65-5-209. The PSC's audit made adjustments to BellSouth's earnings for "out of period items, abnormal and unusual expenses and known changes" to reflect an estimate of what BellSouth's earnings would have been on a going forward basis. A stay of the PSC's decision was ordered by the Court of Appeals on February 27, 1996.

The Court of Appeals issued its decision on October 1, 1997, finding that the audit prepared by the PSC exceeded its authority under the statute and that if the PSC had not made improper adjustments BellSouth's earnings would have been within the range. The Court of Appeals remanded the case to the TRA to place BellSouth under price regulation. BellSouth, however, petitioned the Court of Appeals for a rehearing for the purpose of asking the Court to fix the effective date of the price regulation plan as March 1, 1996. The Court of Appeals denied this petition on November 19, 1997, finding that it was the responsibility of the administrative agency to fix the effective date.

Then, on January 20, 1998, the TRA and the Attorney General's Consumer Advocate Division filed an application for permission to appeal with the Tennessee Supreme Court of Appeals. The Supreme Court denied the application on June 15, 1998, and on June 29, 1998, the Court of Appeals issued its mandate to the TRA.

After this final mandate, the Authority received legal briefs from the parties on how the Authority should proceed. On October 27, 1998, consistent with the Court of Appeals mandate, the Authority placed BellSouth under price regulation effective October 1, 1995. However, the price freeze on basic residential and call waiting services will not expire until December 1, 2002. The TRA's Order in this proceeding can be found in Appendix B.

Price regulated companies are allowed to increase rates for one service while decreasing rates for another as long as the aggregate revenues are not increased. For example, in 1996, Sprint/United implemented a \$.29 directory assistance charge while reducing switched access charges to long distance companies. After intervention by the Consumer Advocate Division of the Tennessee Attorney General's Office, an extensive hearing was held. The Authority found that the General Assembly did not intend for directory assistance to be construed as a basic service in the statute and that the \$.29 directory assistance charge is permitted as a matter of law. Nevertheless, the TRA increased the monthly free call allowance from the three (3) calls proposed by the company to six (6) calls and exempted disabled persons from directory assistance charges. In addition, persons over 65 years of age were exempted upon request. Appeal of this decision is pending before the Tennessee Court of Appeals.

In 1997, Sprint/United proposed increases to residential ISDN rates, call forwarding, and operator assisted calls while reducing business ISDN rates and switched access charges to long distance companies. After testimony and hearings on this matter, the Authority denied Sprint/United's adjustment, finding that residential ISDN is a basic service and that Sprint/United's rates for this service cannot be increased until the October 15, 1999, pursuant to state statute.

Sprint/United currently has a filing pending proposing increases to intraLATA long distance rates in the Tri-cities area and northeast Tennessee, and increases to Caller ID and Call Forwarding services. The company is proposing to offset these increases with reductions to the rates for dedicated private lines to business customers and custom calling packages. The Consumer Advocate has intervened in this proceeding, but has agreed to allow Sprint/United to place the rates into effect subject to refund if not approved by the TRA. A hearing on this filing is pending.

**SIGNIFICANT DECISIONS SINCE THE PASSAGE OF THE TENNESSEE
TELECOMMUNICATIONS ACT OF 1995**

		1995		
Tennessee Telecommunications Act of 1995 passed.	6/06/95		6/13/95	Long Distance and Reseller Rules become effective.
Sprint/United & BellSouth file for Price Regulation.	6/19-20/95		8/24/95	Four companies are granted authority under the state statute to provide competitive local telephone service.
Sprint/United's petition to enter into price regulation is approved.	10/15/95		12/19/95	PSC finds that Tennessee universal service fund is not needed at this time, due to lack of competition.
		1996		
PSC promulgates rules establishing Small & Minority Telecommunications Business Assistance Program.	1/02/96		1/23/96	PSC approves BellSouth's petition to enter into price regulation, after reducing rates by \$56.3 million. Appealed by BellSouth.
Federal Telecommunications Act of 1996 signed into law.	2/08/96		2/27/96	Tennessee Court of Appeals stays the PSC's Order of January 23, while considering BellSouth's appeal.
Citizens Telecom's petition to enter into price regulation is approved.	4/12/96		6/28/96	PSC approves Interconnection Agreements between BellSouth and three Competitive Telephone Companies.
Tennessee Regulatory Authority (TRA) commences operations.	7/01/96		7/17/96	AT&T files petition with TRA for arbitration of its interconnection agreement with BellSouth.
MCI files petition with TRA for arbitration of its Interconnection agreement with BellSouth.	8/16/96		9/20/96	Sprint files petition with TRA for arbitration of its Interconnection agreement with BellSouth.
TRA grants Sprint/United authority to provide interLATA long distance services.	11/12/96		11/25/96	TRA issues its First Order of Arbitration Awards in the AT&T, MCI and BellSouth Interconnection Agreement. Establishes proxy rates for network elements.

Table 11

SIGNIFICANT DECISIONS SINCE THE PASSAGE OF THE TENNESSEE TELECOMMUNICATIONS ACT OF 1995

		1997	
TRA establishes wholesale discounts that BellSouth and Sprint/United must offer to local service resellers.	1/17/97	4/15/97	TRA approves Sprint/United's interLATA toll dialing parity plan. This allows customers of Sprint/United to choose an intraLATA long distance carrier.
TRA approves the price regulation indexing formula in accordance with T.C.A. § 65-5-209.	5/20/97	5/20/97	TRA finds that as a matter of law, Sprint/United can begin charging for Directory Assistance. A monthly call allowance of six free calls per customer is approved. This decision was subsequently appealed by Sprint/United and the Consumer Advocate. The Court of Appeals Decision is pending.
TRA approves tariff by Sprint/United to offer collocation to competing carriers.	7/29/97	8/05/97	TRA approves Citizens Telecom's IntraLATA Equal Access Implementation Plan. This plan allows customers of Citizens Telecom to choose their provider of intraLATA long distance service.
As permitted under the FCC's deregulation of payphone rates, the rate of a payphone call is increased from \$.25 to \$.35.	9/01/97	9/23/97	TRA finds that BellSouth must allow competing telecommunications providers to have their company's name on the cover of the white page directory. Appealed by BellSouth. Decision is pending.
		1998	
TRA denies petition of Hyperion of Tennessee, a competitive local exchange company, challenging T.C.A. § 65-4-201 which protects small incumbent telephone companies from competition. Hyperion later appealed this decision to the FCC where it is pending.	3/10/98	3/24/98	TRA issues its first ruling on the creation of an intrastate universal service fund. The Authority rules on 52 issues and sub-issues that define universal services and the parameters for identifying implicit subsidies.
In a complaint filed by Brooks Fiber, a competitive local exchange carrier, the TRA orders BellSouth to pay Brooks Fiber interconnection fees on calls made by BellSouth customers to Internet service providers served by Brooks Fiber. BellSouth appeals this decision to Federal Court where a decision is pending.	6/02/98	6/15/98	TRA promulgates Local Telecommunications Competition Rules as required by T.C.A. § 65-4-124 are approved.
The TRA rules on Sprint/United's second Annual Price Cap Adjustment. The Authority denies Sprint/United's request to increase residential ISDN rates. TRA finds that ISDN is a basic service that is frozen until October 1999 in accordance with T.C.A. § 65-5-209.	6/30/98	6/30/98	The Authority issues its first decision in the docket created to establish cost based rates for unbundled network elements as required by the Federal Telecom Act. The Order addresses 19 issues involving the cost methodology and assumptions to be used in calculating the cost of unbundled network elements.
TRA opens a docket to study the competitive impact of contract service arrangements filed by BellSouth	7/07/98	9/15/98	TRA grants BellSouth Enterprises (BSE), an affiliate of BellSouth Telecommunications, authority to offer intraLATA services, as permitted by law, in areas outside of the service area of BellSouth Telecommunications.
TRA orders BellSouth to include NextLink's name on the cover of the white page directory for Nashville. BellSouth has appealed this decision.	10/15/98	10/19/98	Sprint/United files its third annual price regulation adjustment. Its proposal includes rate increases for intraLATA long distance and custom calling features. A hearing and decision by the Authority is pending.
Subsequent to the Tennessee Supreme Courts decision not to hear the appeal of the decision by the Court of Appeals on the BellSouth price regulation petition, the TRA places BellSouth under price regulation effective October 1, 1995.	10/27/98	11/17/98	In a status conference conducted by the TRA, the parties stipulate that BellSouth meets 3 of the 14 checklist items outlined in Section 271 of the Federal Telecom Act required for BellSouth to provide interLATA long distance services. The remaining checklist items are under review by the Authority.
The TRA conducts a show cause proceeding to determine if Minimum Rate Pricing, a reseller with 132 slamming complaints filed against them, should be fined and lose its certification. A decision is pending.	11/24/98	12/17/98	The Authority revises its rules to impose significant penalties on companies that fraudulently change a consumers long distance carrier or bill for services not requested by customers (Slamming and cramming).

Table 11

THE STATUS OF LOCAL COMPETITION IN TELECOMMUNICATIONS

E. Small And Minority-Owned Business Plans

T.C.A § 65-5-212 requires telecommunications service providers to provide the TRA with their plans to purchase goods and services from small and minority-owned telecommunications businesses. Each plan is reviewed by the TRA when a company makes its request for certification. The companies are also required to submit information on existing programs designed to furnish technical assistance to small and minority-owned telecommunications businesses.

The statute defines a small and minority-owned business as “a business which is solely owned, or at least 51% of the assets or outstanding stock of which is owned, by an individual who personally manages and controls the daily operations of such businesses, and who is impeded from normal entry into the economic mainstream because of race, religion, sex, or national origin, and such businesses have an annual gross receipts of less than four million dollars.”

The TRA has conducted an evaluation of the Small and Minority-Owned Business Plans of telecommunications providers. Below is our review:

1. Evaluation of Small and Minority-Owned Business Plans of Telecommunications Service Providers in Tennessee

T.C.A. § 65-5-212 requires each telecommunications service provider to file with the TRA a small and minority-owned telecommunications business plan (hereafter referred to as the “Plan”). The Plans were to be filed with the Authority by August 6, 1995, for existing telecommunications companies and at the time of application for a certificate for new telecommunications providers.

The purpose of the statute is to ensure that no group is excluded from participating in the telecommunications sector because of race, religion, sex or national origin. The statute requires the Plans to describe how the provider intends to purchase goods and services from small and minority-owned telecommunications businesses and provide

information on technical assistance programs available to these businesses. The statute defines a small business as one with annual gross receipts of less than four million dollars (\$4,000,000).

In an attempt to evaluate the effectiveness of the companies' Plans, telecommunications companies required to file small and minority-owned plans under TCA § 65-5-212 were sent a survey asking the following questions:

1. Identify the contract opportunities that exist with your company for small and minority-owned telecommunications companies.
2. Does your company maintain a list of small and minority-owned telecommunications businesses that are eligible for opportunities with your company?
3. What methods does your company employ to identify small and minority-owned businesses?
4. What methods does your company use to notify small and minority-owned businesses of opportunities within your company?
5. What is your company's projected dollar amount of contracts to small and minority-owned businesses for 1997?
6. Provide a list of the actual number and the dollar amount of small and minority-owned business contracts your company entered into during 1996 and 1997.
7. Describe any programs in which your company provided technical assistance to small and minority-owned businesses during 1996. Also, provide the number of times the programs were utilized during 1996 and 1997.
8. Provide the name and address of the company official responsible for the implementation of the Small and Minority-Owned Business Participation Plan.

Of the thirty-eight (38) companies sent surveys, seventeen (17) were incumbent local exchange carriers ("ILECs"), five were interexchange carriers ("IXCs") and the remaining sixteen (16) were competing local exchange carriers (CLECs). The surveys were mailed on August 1, 1997, and a follow-up reminder was sent out on September 29,

1997, to those companies that failed to respond. At the present time, only one (1) company has failed to respond to the survey.

Seven (7) companies responded that they had not taken any steps to implement their small and minority-owned business plans because of delays in beginning business in Tennessee. Below is a list of the companies that responded and those that did not respond:

Companies Responding to Survey

Sprint Communications Company LP	Tennessee Telephone
Loretto Telephone Company	Concord Telephone
Citizens Telecom	Tellico Telephone
DeltaCom, Inc.	Humphreys County Telephone
Time Warner Communications	CenturyTel of Adamsville
AT&T Communications	Peoples Telephone
Winstar Wireless of Tennessee	Crockett Telephone
Sprint/United	West TN Telephone
LDDS WorldCom	Citizens Telecom of TN
BellSouth Telecommunications	United Telephone Co.
CenturyTel of Claiborne	Ardmore Telephone Co.
CenturyTel of Ooltewah-Collegedale	Comm Depot Inc.
ATS of Tennessee Inc.	GTE Long Distance
Intermedia Communications Inc.	NextLink of Tennessee
Brooks Fiber Communications of Tennessee.	MCI Telecommunications
ICG Telecom Group Inc.	Frontier Communication
Metropolitan Fiber Systems of TN	LCI International
Millington Telephone Company	Citizens Telecommunications
Southeast Telephone LP	of the Volunteer State

Companies Not Responding to Survey

Hyperion of Tennessee Inc.

Below is a discussion of the results of the survey. The results of each question will be reviewed along with some analysis. This section will conclude with a summary of the results of the survey.

1. **Identify the contract opportunities that exist with your company for small and minority-owned telecommunications companies.**

Twenty-five (25) companies responded that opportunities exist with their companies for telecommunications contractors. This potential is being influenced by telecommunications companies' trend toward outsourcing certain functions for the purpose of making their operations more efficient.

The largest area for potential work is in the area of outside plant construction. Seventeen (17) companies stated that they use contractors for the construction of new outside plant such as the installation of fiber optic cable. The next highest category for contracting is in the area of professional services. Such functions in this category include tax compliance, information systems support and engineering. Finally, the purchase of central office equipment is identified as an area in which telecommunications companies seek bids.

Eleven (11) companies cited the lack of opportunity at the present time. However, eight (8) of these companies stated that they had either just started doing business or had not yet begun doing business in Tennessee.

2. Does your company maintain a list of small and minority-owned telecommunications businesses that are eligible for opportunities with your company? How often is your list updated?

Twenty-six (26) companies reported that they do not maintain a list of small and minority-owned telecommunications businesses. Many of these companies stated that they have had trouble locating such a list. Only ten (10) companies maintained such a detailed list. These ten (10) companies stated that the updating of their list was done at varied intervals ranging from monthly to yearly.

3. What methods does your company employ to identify small and minority-owned businesses?

Eleven (11) companies stated that they have not taken steps to identify these potential businesses. The majority of these companies seven (7) indicated that no steps have been taken because they are not currently doing business in Tennessee. Twenty-one

(21) companies stated that they take active steps to identify small and minority owned businesses. Some of the most popular sources or methods includes:

- Local Chambers of Commerce
- Tennessee Economic Community Development Department
- Trade fairs
- Advertising in minority publications
- Service on Boards of organizations such as the NAACP and the Urban League
- Small Business Administration's Procurement Automated System (PASS)

4. What methods does your company use to notify small and minority-owned businesses of opportunities within your company?

Nineteen (19) of the thirty-seven (37) companies responding stated that they do not specifically notify small and minority-owned businesses of business opportunities within their company. Several of these companies stated that they maintain a general list of qualified vendors which does not specify whether the vendor is a small or minority-owned business.

Sixteen (16) companies stated that they have processes in place to notify such businesses. The most common method of notification was by mail requesting bids.

5. What is your company's projected dollar amount of contracts to small and minority-owned businesses for 1997?

Twenty-four (24) companies indicated that they did not anticipate any contracts for small and minority-owned business during 1997. Only eleven (11) companies stated that they had existing contracts with small and minority-owned businesses during 1997. These companies tend to be the larger multi-state corporations like Sprint, MCI, BellSouth and AT&T. Total nation-wide dollar amounts projected in these contracts for 1997 amount to approximately \$3.2 billion.

It was difficult getting Tennessee specific dollars spent by Tennessee telecommunications service providers on contracts to small and minority-owned

businesses. BellSouth, Sprint and MCI, for example, stated that they do not track state specific dollars for this category and were unable to provide the information. The eight (8) companies that did track Tennessee specific dollars for this category reported a total of \$6,746,190 was projected to be spent during 1997 on small and minority-owned business contracts in Tennessee. Loretto and Millington telephone companies led the small ILECs with each spending \$500,000 on small and minority-owned business contracts during 1997.

One interesting conclusion of the survey was the dollar amount invested by new CLECs in small and minority-owned businesses. Two (2) CLECs (Intermedia and Time-Warner) reported that they projected spending \$692,000 for contracts with small and minority-owned businesses during 1997.

6. Provide a list of the actual number and the dollar amount of small and minority-owned business contracts your company entered into during 1996 and 1997.

Sixteen (16) companies presently doing business in Tennessee reported that they had no contracts with small and minority-owned businesses during 1996 or 1997. Eight (8) additional companies stated that they had no such contracts during this period of time because they were not providing service in Tennessee. These companies were newly approved CLECs. Eleven (11) companies reported that they had at least one (1) contract with small and minority-owned businesses during this period of time. Sprint/United reported that it had 152 contracts with small and minority-owned businesses that totaled over \$2 million. BellSouth reported having 31 such contracts but refused to submit the dollar amount of these contracts claiming their proprietary nature.

7. Describe any programs in which your company provided technical assistance to small and minority-owned businesses during 1996. Also, provide the number of times the programs were utilized during 1996 and 1997.

Few companies indicated that they have technical assistance programs for small and minority-owned businesses seeking to enter the telecommunications field. Only seven (7) companies reported that they either have a stand alone program to assist small and

minority-owned businesses or that they are a part of such a program sponsored by another organization. Some small ILECs indicated that they participate with local Chambers of Commerce to assist small businesses.

8. Provide the name and address of the company official responsible for the implementation of the Small and Minority-Owned Business Participation Plan.

Of the companies responding, only Brooks Fiber, Frontier and WinStar failed to identify the name and address of their company official responsible for implementing their small and minority-owned participation plans.

Conclusion of Survey

This evaluation of the small and minority-owned business plans of telecommunications providers indicates that little progress has been made in implementing the plans on file with the Authority. Only eleven (11) companies out of the thirty-eight (38) surveyed indicated that they awarded at least one (1) contract to a small and minority-owned business during 1996 and 1997. The major factor for the lack of activity in this area for CLECs is the failure of these businesses to begin operations in Tennessee. However, the survey does indicate that some companies are making efforts to establish business contacts with small and minority-owned businesses.

It appears that existing companies such as BellSouth, AT&T, MCI and Sprint/United have well-established programs that are showing significant activity. Even some small ILECs such as Loretto, Millington, United Telephone and Ardmore appear to be making an effort to contract services to small and minority-owned businesses.

T.C.A. § 65-5-212 requires companies to file copies of their plans along with annual updates with the Authority. All ILECs and CLECs have filed Plans with the TRA. A copy of this survey has been shared with the Department of Economic and Development's Office for Small Business, Entrepreneurship and Minority Affairs.

IV. STATUS OF UNIVERSAL SERVICE IN TENNESSEE

Universal service is the provision of “residential Basic Local Exchange Telephone Service at affordable rates” (T.C.A. §65-5-207(a)). The success of universal service policies are assessed using the penetration rate of residential telephone service, or the percentage of households with telephone service in a given area. Since 1990, Tennessee’s rate has been statistically indistinguishable from the national rate, 94.1% of households having telephones in March 1998.

When examined more closely, however, considerable variation in the proportion of households with telephones is evident across the state. Table 12 shows Tennessee telephone penetration rates by county from the 1990 U. S. Census. Some urban counties approach 100%, while some rural counties barely achieve 80% penetration rates. This occurs despite the lower telephone rates in rural areas set specifically to encourage higher telephone penetration in those areas.

Overall, Tennessee performs as well as the nation as a whole, but room remains to improve universal service. State and federal universal service policy developments are described below.

A. State Universal Service Proceedings

In an attempt to boost universal service, local telephone rates are generally lower in rural areas than in urban areas, even though the cost of providing telephone service is higher in rural areas on average. This presents a dilemma for competitive entry in rural areas, as prices may not provide enough revenue to cover entrants’ costs. To encourage competitors to serve residential customers throughout the state without raising monthly telephone rates, Tennessee’s Telecom Act provided for a special fund to subsidize residential telephone service in high cost areas. The State Act also gave the TRA the ability to consider such a fund, while the federal act establishes a national mechanism under the FCC, but allows states to establish their own system as well. In its Order of December 19, 1995, the PSC found that such a fund was not needed in Tennessee at that

time due to lack of competition. The TRA opened a docket to review universal service in Tennessee on May 13, 1997. Moving in parallel with national proceedings before the FCC, this docket considers universal service funding for non-rural carriers only. Rural telephone companies service territories will be considered when competitive entry to those areas is allowed.

The TRA's universal service proceeding is divided into three (3) phases. The Interim Order on Phase I, on cost issues, was issued on May 20, 1998. Hearings on Phase II have been held and the TRA's decision is pending. Phase II deals with the determination of the costs and revenues associated with providing universal service at the telephone company wire center level. Phase III will consider proposed rate changes in light of the Phase II costs and revenues analysis. This will determine the size of the Tennessee universal service fund. Implementation of a Tennessee fund depends on the conclusion of the FCC's proceeding on national universal service funding.

B. Federal Universal Service Proceedings

The federal act mandates consideration by the FCC of revisions to its universal service support mechanisms. On May 8, 1998, the FCC issued its Report and Order on Universal Service. Subsequently, the FCC's findings on the revenue base on which to assess contributions to the fund have been appealed. Several issues have been referred to a special Federal-State Joint Board on Universal Service, and the FCC has developed a cost model to use in identifying high-cost areas served by non-rural companies. The FCC has set July 1999 as its target for implementation of the new federal mechanisms, although this date depends partly on the outcome of pending appeals.

The federal act also establishes new programs to support access to advanced telecommunications service for schools, health care, and libraries. Funding for these programs is provided by interstate long distance carriers. The FCC has allowed these carriers to recover the funding requirements from their customers. As a result, some

carriers have added a fixed monthly charge to customers' bills. These charges are under reconsideration by the FCC at this time.

Percent of Households with Telephone Service



Table 12

V. AVAILABILITY OF TELECOMMUNICATIONS SERVICES AND TECHNOLOGICAL CHANGES IN THE MARKETPLACE

A. Availability of Telecommunications Services and “The Last Mile”

As discussed previously, local telephone service from competing providers is generally available in some form to business customers in the state’s four (4) largest metropolitan areas. These competing providers are offering comparable services to the incumbent providers (i.e., local service, custom calling features, data services and intraLATA long distance services). In addition, CLECs are packaging their local services with long distance services.

One of the main reasons that local telephone competition is limited is because competitors are having to lease the local loops of the incumbent providers. This local loop, the wire between the customer’s premise and the telephone company’s central office, is frequently referred to as “the last mile.” It is not economically feasible for competing providers to duplicate this wire network because of the large capital expenditures required to construct these loops. These expenditures include the cost of poles, conduits, rights-of-way, trenching costs and cable costs including associated labor. Competing providers are currently investing billions of dollars nationally to develop new technologies to compete with the “last mile” of the incumbents. For example, AT&T recently purchased TCI, one of the nation’s largest cable television providers for \$30 billion. This merger will give AT&T access to 10 million residential households nationwide via the coaxial cable currently used to provide cable television service. AT&T has also announced a partnership with Time Warner for use of Time Warner’s coaxial cable serving consumer households. AT&T estimates that it will have to spend \$10 billion to equip the coaxial cable to provide the two-way communications needed for telephony (cable television is currently only one-way communications). Microsoft is also making substantial investments in cable television and the cable modems used to provide high speed Internet access. Microsoft President Bill Gates has indicated on numerous occasions that antiquated telecommunications networks are holding back the computer industry.

Wireless technologies such as cellular, personal communications services (PCS), microwave and satellite are also the focus of many competing providers in search of an economic alternative to the incumbent's "last mile." Cellular and PCS services are generally available today, but current prices of these service do not make them viable alternatives to the incumbent's wireline service. For example, digital cellular service generally costs about \$20 per month for 100 minutes while wireline service costs about \$17 per month (in metropolitan areas) for unlimited usage.

Also, competing carriers are examining microwave and satellite technologies for providing wireless alternatives to the "last mile." Teligent Communications has invested \$800 million in developing telecommunication services for small business subscribers using satellite microwave dishes. NextLink and Microsoft are also investing heavily in satellite technologies.

Until economically viable alternatives to the incumbents "last mile" are developed and functioning, many industry experts contend that local telephone competition will not be able to flourish. The remainder of this section discusses in more detail these technological changes.

<u>"The Last Mile"</u>	
◊	The incumbent companies own the majority of the wires going into each home and business ("the last mile").
◊	In many cases, competitors are having to rent the "last mile" from the incumbent (its competitor) in order to compete.
◊	Many potential competitors are looking for alternatives to using incumbent loop. <ul style="list-style-type: none">- Wireless - Microwave (Teligent)- Wireless - Cellular and PCS- CATV (AT&T)- Satellite (Microsoft and NextLink)
<i>Table 13</i>	

B. Changing Technologies

The existing telephone network was constructed to provide voice communications to consumers. In 1988, voice communications comprised approximately 80% of the traffic on the telephone network, with data comprising 20% of the traffic. Yet, over the past 10 years, data traffic on the network has constantly increased to the point that today data exceeds voice traffic. This has caused providers to re-examine their networks and search for new technologies that will enable them to meet the increasing data needs of today's consumer.

Some say that the transformation of the telecommunications industry we are seeing today all started with the Internet. Although the Internet is sure to become a historical point of reference, what is now happening in telecommunications is not only about the Internet or even about the recent surge in data networking. It is about the progression of new applications, new ways to communicate and new ways to transport information, whether that information is data or voice. It is also about the role the various carriers have in facilitating that progression. It is about the integration of many services such as voice, data and video into the same network "pipe." It is about competition and how the many carriers and the industry as a whole function together. In the presence of all this and what is making it all possible are the rapidly changing technologies that the various carriers use to provide their services to the consumer.

Physical Facilities

The most forward-looking technology in telecommunications transmission continues to be fiber optic cable. The main reason for this is that technology continues to expand the information carrying capacity and transmission speed of fiber. Additionally, some of this same expanded capacity and speed can now be utilized in much of the traditional twisted copper pair telephone plant that comprises much of the "last mile" of the network.

Fiber Optics

The constant demand for higher capacity and speed of data transmission have led to the use of new optical networking methods that are now being used by carriers to delay reinforcement and/or replacement of fiber plant. These methods include technology like wavelength division multiplexing (WDM). Essentially, WDM allows carriers to combine multiple paths of light carrying both voice and data transmission onto a single optic path. This technology is creating both cost and capacity efficiencies by allowing higher volumes of traffic to be transported over the same amount of fiber. In the 1980's, the technology of the day allowed two (2) channels or paths over a fiber system. This capacity grew to four (4) channels in the early 1990's and to 16 or more in 1996. Present technology has enabled that number to increase to 40 optical channels that are available today. Laboratory tests have successfully transmitted information at the rate of 2 trillion bits (2 terabits) per second using this technology. To illustrate how powerful this technology can be, a 2 terabit capacity network would have the capacity to transmit the entire Library of Congress coast to coast in 20 seconds. This capacity will soon be possible with some networks carriers now have under development.

Digital Subscriber Lines

The last component of most facility-based carrier networks is the copper loop, a pair of copper conductors or wires, that connect customers to central offices and the backbone network. This copper loop was designed and constructed to carry voice signals. Existing carriers have little incentive to replace this last piece of the network with fiber optics because of the large amount of capital they have invested. Instead, they are basically looking for solutions that will allow them to evolve the local loop to higher capacities until the implementation of more advanced technologies become cost effective. Digital subscriber line (DSL) offers these benefits to carriers by using existing wiring to expand the capability of existing copper plant to support high speed data and voice services. Two types of DSL technology that are now seeing prevalent use are high bit-rate DSL (HDSL) and asymmetrical DSL (ADSL). Carriers are now able to deliver 1.5 million

bits of information per second over the local network with the use of DSL technology. DSL can support a wide variety of high bandwidth applications such as high speed Internet access, telecommuting and private networking. DSL is being deployed by carriers nationally and in Tennessee as well.

Packet Networks

As carriers address the access and transport issues brought on by the vast increase of data traffic, they are also adding more intelligence and flexibility to their switching networks to manage and direct the traffic. Future networks must efficiently transport huge amounts of data. By the year 2007, industry experts estimate that data traffic will require more than 20 times the bandwidth of voice traffic. Carriers are planning a new generation of networks and are upgrading existing networks for operation beyond the year 2000.

Data transfers over networks tend to be “bursty” in nature. That is, it tends to bunch up in blocks. For example, an Internet user may spend a few seconds downloading a web page and then the next several minutes reading the information. Much of the time the connection between the user and the web host remains unused. Contemporary networks reserve time slots and space throughout the entire network for the duration of any connection even if there is no data to transfer. This is similar to a typical voice conversation where there are pauses and silent periods in the conversation but the connection or circuit is still active and no one else can utilize it. This type of network connection is extremely inefficient for data transmission. Suppose the unused portion of the network “space” or bandwidth could be used by another user so more than one could be accommodated on the same network element at the same time. This is exactly the principle used in “packet” or cell-based networks that share bandwidth across many users. End users get a portion of the bandwidth when they actually need to transmit a piece of information. The rest of the time, the bandwidth is available for other users. This allows for high network usage and efficiency. At this time, however, voice traffic over packet networks is limited.

As the next century approaches, an evolution of networks will be required to efficiently utilize available bandwidth. One type of "packet switching" is called asynchronous transfer mode (ATM). In ATM, information is organized into cells. It is called asynchronous because the recurrence of cells containing information from an individual is not necessarily periodic. ATM becomes increasingly crucial for carriers as they merge different traffic types (i.e., voice, data, video) at multiple points in the network. ATM is allowing carriers to move toward one multi-service network rather than maintaining different network types to perform various functions.

Wireless Communications

Although wireless providers are not regulated by the TRA, the potential they offer for competing with services offered by regulated carriers in Tennessee makes it important for the TRA to monitor this rapidly changing technology. Wireless technology includes microwave, cellular telephone, paging and PCS.

Microwave

Microwave technology has been used for a number of years to transmit voice and data from one point to another on the traditional toll network. Carriers have now started using microwave radio to build digital broadband point to multipoint local networks. Already one such carrier, Teligent, has been granted approval to operate as a CLEC in Tennessee and plans to target small to medium-sized business in ten (10) counties around Nashville and Memphis. Teligent has raised \$850 million in capital to deploy this technology nationwide. High quality, low cost, high bandwidth transmission of integrated packages of voice, data, Internet, and video conferencing is possible using this medium.

Networks of this type are comprised of microwave antennas located atop customers' premises connected to a central communications node via a microwave radio signal where it is received by a base station. A typical distance between a customer building and the node might be on the order of three (3) miles. Using this technology, many customer buildings can point and transmit to a single node. The node connects the

telecommunications traffic to the service provider's switch, either through another wireless connection, or via fiber from another carrier. At the switch, the traffic is handed off to the appropriate interconnect carrier for call completion.

Cellular

Cellular service uses one or more multichannel base stations to provide radio telecommunications services to mobile stations over a wide area. Cellular systems employ techniques such as low transmitting power and automatic hand-off between base stations to enable channels to be re-used in relatively short distances. There are two (2) types of cellular service that are currently offered. Analog cellular was originally devised in the late 1970's and early 1980's. Some of the shortcomings of analog cellular such as low calling capacity, poor data communications and minimal privacy are being addressed by the deployment of new digital systems. The advantages of digital cellular technologies over analog cellular include increased capacity and security. Technology now exists to expand the capacity of cellular systems 15 times what is possible with analog systems. Additionally, digital cellular signals are now easily scrambled to provide a degree of privacy not available in analog systems. Because of the enormous amount of money cellular providers have invested in analog technology, many providers are converting to digital by overlaying their existing networks with the new technology and keeping the same frequency and channel allocations. This type of conversion is providing many of the benefits of digital transmission at a lower cost to the consumers.

PCS

Personal communications services (PCS) is a new generation of wireless-phone technology that introduces a range of features and services that surpass those available in analog and digital cellular phone systems. PCS provides the user with an all-in-one wireless phone, paging and data service with greatly improved security. Increasingly, PCS providers are opting for a new hybrid approach to service that combines mobility with a fixed application. Trials are now being developed in various parts of the U.S. whereby PCS carriers will enter the wireless local loop (WLL) market in combination with their

more traditional mobile service. By doing this, they will make the most of their expensive PCS licenses. Using this approach and a single number philosophy, end users will be able to migrate from mobile to fixed using one number that is tied into a single voice mail system. Appendix G lists the cellular and PCS providers operating in Tennessee.

Satellite

Satellite based wireless telecommunications systems are now being deployed to provide voice, data, fax and other telecommunications services to users worldwide. Users will make or receive calls using hand held or vehicle mounted terminals similar to cellular telephones. Calls will be relayed through satellites, to a ground station and then through local terrestrial wireline or wireless systems to their end destinations. Some systems will use a telephone that works in two modes. As a wireless phone, it will seek out available service from existing land based networks. In this way it will operate the same as wireless systems now in existence. When wireless service is not available, the user can switch the phone to satellite operation. The call is then relayed from satellite to satellite, until it reaches its destination: either through a local gateway and the public switched telephone network, or directly to a receiving phone. The satellites also keep track of the user's telephone location anywhere on the globe. This will allow the user to do such things as find a lost car in the parking lot, continually monitor traffic conditions and road construction enroute to a destination and even receive turn by turn directions to an ultimate destination. This same technology will also allow for the quick location and recovery of stolen vehicles. Today, satellite telecommunications is only available on a very limited basis.

VI. FEDERAL TELECOMMUNICATIONS INITIATIVES

A. Overview of Federal Telecommunications Act of 1996

This act seeks, “to promote competition and reduce regulation in order to secure lower prices and higher quality services for American telecommunications consumers and encourage the rapid deployment of new telecommunications technologies.” To this end, the Act requires local telephone companies to open their networks for interconnection with other providers and for the resale of local telephone services. State regulators may arbitrate disputes between incumbents and entrants should they fail to agree on interconnection arrangements. The TRA has approved twenty-one (21) interconnection agreements between competing carriers of which four (4) were arbitrated.

The Act also prohibits the creation of barriers to entry by the states and requires the removal of barriers to infrastructure investment. The latter is intended to promote the availability of advanced services to all telephone users. The Act suggests the use of alternative regulatory forms, such as price regulation, in order to encourage investment in new technologies.

As soon as the local markets served by the regional Bell Operating Companies (BOCs), such as BellSouth, are sufficiently open to competitors, the Act allows the BOCs to provide long distance service within their home regions, a service they have been barred from providing since the AT&T divestiture in 1984. The FCC, with advice from the Department of Justice and state regulators, decides whether the requirements of the Act in this regard are satisfied on the state-by-state applications of each BOC. Such applications for Michigan, Oklahoma, South Carolina, and Louisiana (twice) have come before the FCC to date and all have been rejected.

B. FCC Decisions

Interconnection

The FCC issued its Order on interconnection requirements and pricing methodology for the unbundled piece parts of local telephone networks in August 1996. Several states and some BOCs challenged parts of the FCC's Order in federal court. The Eighth Circuit Court of Appeals found that the FCC exceeded its authority in imposing pricing rules on the states and by requiring incumbents to combine some of the unbundled parts of their networks for competitors. However, the United States Supreme Court recently overturned the Eighth Circuit's decision and reinstated a portion of the FCC's rules.

Access Charge Reform

The FCC issued its Order revising the regulatory scheme under which local exchange carriers assess costs to long-distance and other carriers for use of the local telephone networks to complete interstate telephone calls on May 16, 1997. This Order was appealed by long distance carriers as well as incumbent local telephone companies. The long distance companies claimed that the FCC did not make the transition to competitive access rates quickly enough and is too cautious in its concern for universal service. The incumbent local companies, however, argued that the FCC left them exposed to inefficient competitive entry in the short term. The Eighth Circuit Court of Appeals upheld the Order, agreeing with the FCC that it charted a proper middle course, taking account of the complementary but sometimes diverging goals of competition and universal service support.

C. Other Court Decisions

BellSouth and Southwest Bell have challenged the "competitive checklist" in the Act that the BOCs must meet in order to provide in-region long distance service. As of the end of 1998, both of these appeals have been rejected by the respective Court of Appeals. In January 1999, the Supreme Court declined to hear Southwest Bell's appeal.

D. Mergers

Several BOCs have merged or acquired other incumbent telephone companies since the passage of the Federal Act. SBC, the parent of Southwest Bell, and Bell Atlantic have been the most active of the BOCs. SBC acquired Pacific Telesis and Southern New England Telephone Company, and its merger with Ameritech is pending regulatory approval at this time. Bell Atlantic acquired NYNEX and its proposed acquisition of GTE is pending regulatory approval.

The long distance companies have also been active. WorldCom grew to become the fourth largest long distance carrier largely through acquisitions and is now acquiring MCI, the second largest long distance company. AT&T's acquisition of TCI, a cable TV company, is also pending regulatory approval at this time.

Among carriers certificated in Tennessee, fourteen (14) mergers or acquisitions have been approved by the TRA during 1997-98. Of these, eleven (11) involved resellers only. The remaining three (3) combined a Competing Telecommunications Service Provider with a reseller. None involved the combination of facilities-based providers.

The Federal Telecommunications Act of 1996

Key Provisions

- ◇ Obligations of local telephone companies:
 - Interconnection
 - Resale
 - Number Portability
 - Dialing Parity
 - Access to Rights-of-Way
 - Reciprocal Compensation
 - Collocation
 - Unbundled Access
- ◇ State regulators and the FCC have the responsibility for establishing the regulatory framework that enforce the initiatives of the Federal Act.
- ◇ Other provisions:
 - State Arbitration of Interconnection Agreements
 - Universal Service
 - . High Cost Fund
 - . Schools and Libraries Fund
 - . Rural Health Care Fund
 - Bell Operating Companies entry into long distance (Section 271)
 - . Bell must open network to competitors (14 point checklist)
 - . FCC makes the final decision
 - . State regulatory and Department of Justice are advisors
 - Access to advanced telecommunications services (Section 706)
 - . Regulators shall remove barriers to infrastructure investment

Table 14

VII. COMPATIBILITY BETWEEN PROVIDERS

For multiple providers of telephone services to exist in the marketplace, it is necessary to have compatibility between providers. Both the Tennessee Telecommunications Act and the Federal Telecommunications Act mandate all providers of telecommunications to interconnect their facilities with the facilities of other carriers. The federal act requires state regulators to approve interconnection agreements between providers and arbitrate unresolved issues upon a petition by one of the parties to the agreement.

As of December 31, 1998, the TRA has approved twenty-one (21) interconnection agreements between competing carriers, four of which were arbitrated by the TRA. The TRA is currently arbitrating three additional agreements.

The Federal Telecommunications Act requires interconnection between providers at "any technically feasible point within the carrier's network." The definition of "technically feasible" has been a point of much contention between parties attempting to negotiate interconnection agreements. BellSouth argues that competing providers should only be permitted to interconnect in its central office with the competing carriers equipment isolated from BellSouth's equipment by a wire cage or a separate room. Competing providers argued that the cost of constructing this cage or room is cost prohibitive to the competitors and have requested "cageless" collocation of facilities. The TRA currently has a pending docket to study collocation alternatives.

As previously indicated, competing providers are purchasing network elements from BellSouth in order to provide competitive local telephone service. The Federal Act requires that incumbent providers like BellSouth provide services to competing providers at parity with the service it provides to its own customers. Competing carriers have argued in proceedings before the TRA that BellSouth is not providing service to competitors at parity. Competitors argue that BellSouth's ordering processes, installation times and service quality for competitors is inferior to comparable processes, time and quality that

BellSouth provides its own customers. These allegations are being reviewed as part of BellSouth's application to enter the interLATA long distance market.

VIII. SERVICE PERFORMANCE OF TELECOMMUNICATIONS PROVIDERS

This section will review the quality of service provided by telecommunications providers in Tennessee during the period of 1996 through 1998. Analyzing this period of time will provide insight on the quality of telecommunications services since local competition has been authorized in 1995.

Telephone service is traditionally thought of in two (2) terms: local and long distance services. Long distance service has been opened to competition since 1984 when AT&T was divested from the Bell System. After fifteen (15) years, the long distance market is showing increased signs of competition, as evidenced by the over 250 long distance resale companies certified to do business in Tennessee. The local telephone service monopoly in Tennessee was not lifted until the passage of the 1995 Telecommunications Act by the 99th Tennessee General Assembly. As described earlier in the Report, local telephone competition is still in its infancy in Tennessee with approximately 2% of the access lines in the state being served by competitive local exchange carriers (CLECs).

The focus of this section will be on the quality of service provided by both local and long distance telephone companies. The question posed in this section deals with how does telephone service compare today with the service levels of 1996. Indicators of quality of service will include an analysis of consumer complaints received by the TRA and a review of incumbent local exchange carrier ("ILEC") compliance with the TRA's Service Performance Standards.

A. Trend in Telecommunications Complaints

The overall number of consumer complaints received by the TRA against telecommunications service providers in Tennessee has increased since 1988. But, not only is the number of complaints up, but also the number of providers of telephone service, especially in the long distance market. Today, Tennessee consumers have options for long

distance service that were not available several years ago. The following graph includes all complaints received by the TRA regarding any aspect of intrastate telephone service.

**Telecommunications Consumer Complaint Trend
1988-1998**

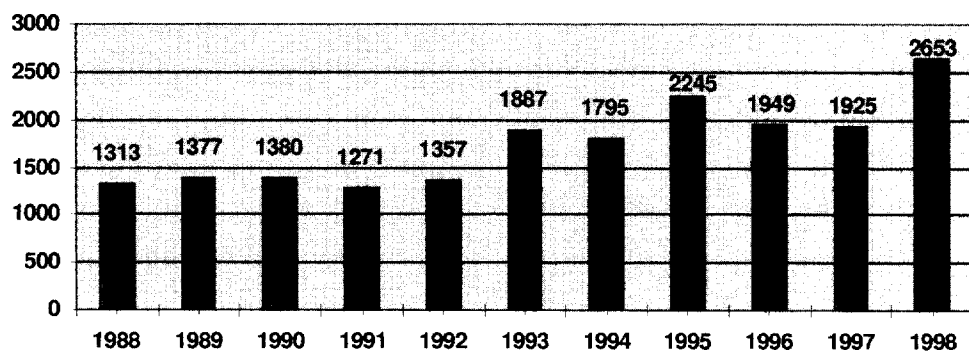


Table 15

The percentage of total complaints received by the TRA against local and long distance and resale companies has increased 100% since 1988. A breakdown of the percent change for each of the three categories since 1996 is listed below:

Percent Change of Consumer Complaints by Industry

	Percentage change in complaints 1996 to 1998
Local Telephone Companies	32% increase
Long Distance Companies	33% increase
Local and Long Distance Resale Companies	42% increase

Table 16

B. Telecommunications Resale Companies

The most significant change in consumer complaints registered against telecommunications companies investigated by the TRA over the past ten years is complaints registered against resale companies. Ten (10) years ago complaints against resale companies were not significant enough to list in their own category. The rapid increase in complaints from this category is one of the main reasons why the trend of telecommunications complaints is dramatically up.

Resale companies tend to be smaller companies with little or no telecommunications facilities. Resale companies purchase network usage from traditional facility-based companies such as BellSouth and AT&T and resell services directly to consumers. TRA records indicate that over 350 local and long distance resale companies are certified to do business in Tennessee. As of the date of this report, the overwhelming majority of resale customers are in the long distance market. Local resale, however, is slowly penetrating the local telephone market, as we predicted in our last Competition Report to the General Assembly.

One niche that local resale companies is meeting in Tennessee is providing local telephone service to consumers with bad credit history. Approximately five (5) resale telecommunications companies in Tennessee are specializing in providing local service to consumers where traditional companies like BellSouth have disconnected due to failure to pay their telephone bills. This service is provided on a pre-paid basis at rates substantially greater than the incumbent providers.

C. Slamming

Another significant factor in the increase of the number in complaints over the last 10 years is the advent of new types of consumer abuses in the telecommunications sector. In 1988, competition in the long distance market was just starting to germinate. AT&T was still the dominate carrier with smaller facility-based companies such as MCI and Sprint attempting to make inroads. As competition started heating up in this segment of

the market, attempts to win customers became more fierce and at times unethical. The drive to add new customers led some long distance companies to switch consumers without proper authorization, a practice referred to as “slamming.” Slamming is by far the fastest growing type of complaint received by the TRA. Over the past seven years slamming complaints grew from 68 complaints in 1991 to 569 complaints during 1998. The majority of slamming complaints received by the TRA are directed against long distance resale companies. Below is a graph illustrating the growth in slamming complaints received by the TRA.

**Trend of Slamming Complaints
1991 - 1998**

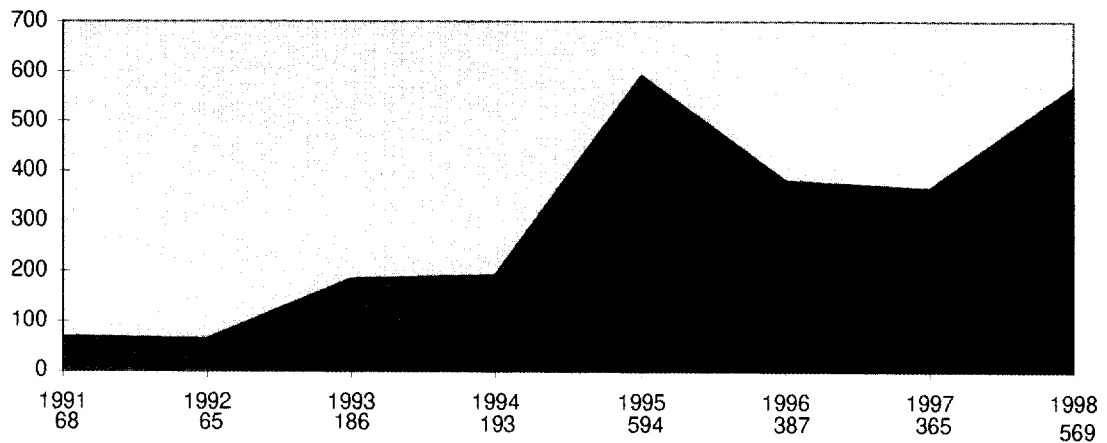


Table 17

In order to address the increase in slamming complaints, the TRA has stepped up its enforcement actions by issuing several show cause orders against long distance companies and resellers. In these proceedings, several of them still in progress, the TRA can issue fines and/or revoke the authority of companies found guilty of slamming. Passage of Public Chapter 709 improves the TRA’s ability to address slamming and cramming in Tennessee.

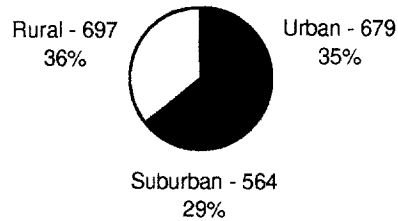
D. Complaint Trend by Geographic Area

As stated in an earlier section, local competition appears to be emerging only in the largest metropolitan areas of the state. No CLEC claims to have customers in any rural area of Tennessee. But while competition is beginning to slowly emerge in these targeted large urban areas, what is happening in other areas of the state where competition is non-existent? A geographic analysis of complaints by urban, suburban and rural areas reveal that the largest growth in consumer telecommunications complaints from 1996 to 1998 was in the suburban areas of the state where competition is miniscale. Below is a graph illustrating the percentage of telecommunications complaints in the urban, suburban and rural areas of Tennessee since 1996.

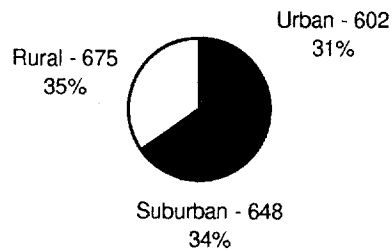
As depicted in the graphs in Table 15, the number of consumer complaints registered against telecommunications companies increased in all three (3) geographic regions of the state since 1996.

Geographical Analysis of Telephone Complaints⁶ 1996 - 1998

1996



1997



1998

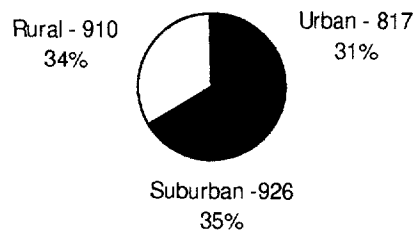


Table 18

⁶ Metro areas include Davidson, Shelby, Knox and Hamilton counties. Suburban areas include all counties touching the metro counties listed above with the addition of Dickson, Madison, Montgomery, Washington and Sullivan counties. Rural areas are all remaining counties.

E. Local Telephone Company Complaint Trend

Consumer complaints against local telephone companies increased by 32% since 1996. Local telephone companies are defined for this analysis only as companies providing local telephone service prior to the 1995 Telecommunications Act. Examples of these companies include BellSouth, Sprint/United, Citizens, etc. Competitive local telephone companies are not included in our analysis here due to their small impact on the local market at this time. Below is a graph illustrating the trend in complaints against local telephone companies by category of complaints since 1996.

**Local Service Telephone Complaint Types
1996 & 1998**

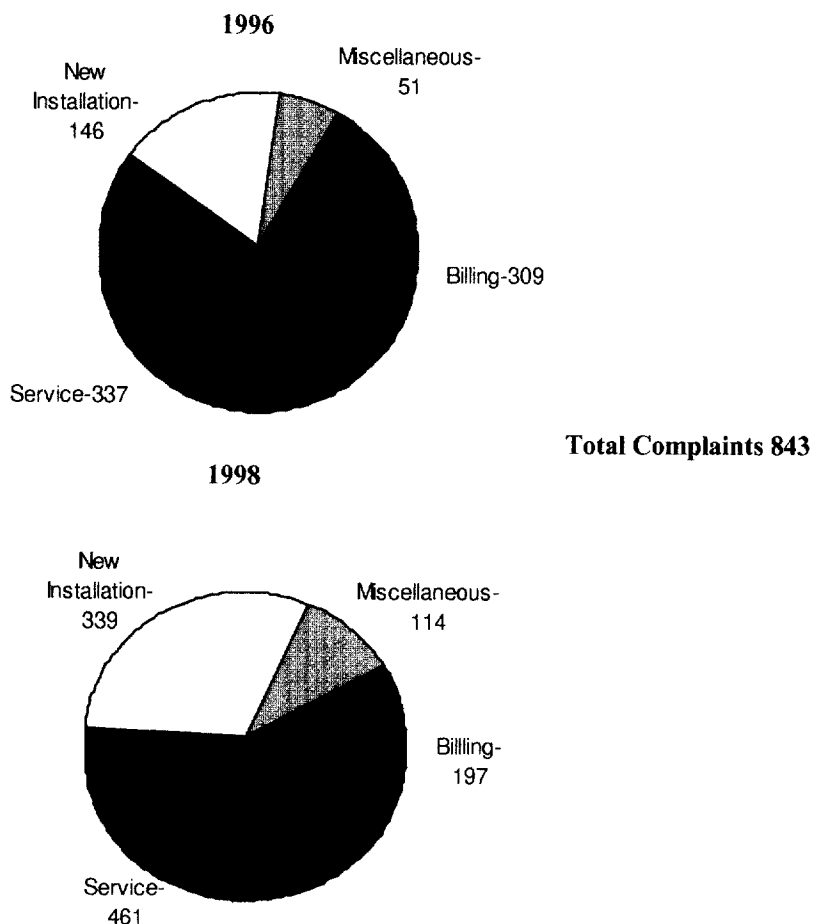


Table 19

Total Complaints 1111

As depicted on the graphs above, the largest increase in consumer complaints against local telephone companies is delays in the installation of new service. This category is defined as consumers having to wait for installation of telephone service due to problems caused by the telephone company. Some of these complaints detail delays exceeding 30 days to receive new service. This category increased 132% since 1996. The TRA is working with these companies to reduce the complaints in delayed service. For example, BellSouth, which had 315 of the 339 complaints in this category, has informed the TRA that it is in the process of hiring over 100 new employees to address this and other service related problems it is experiencing in Tennessee.

The largest category of complaints against local telephone companies is related to service problems such as out-of-order or poor quality of service complaints. This type of complaint increased 37% since 1996. Finally, billing complaints, which typically deal with bill disputes, decreased 36% since 1996.

BellSouth is the largest local telephone company serving 79% of Tennessee access lines. Because of its significant presence, and the fact that BellSouth is the first to face local service competitors, additional analysis on the quality of service of BellSouth is provided. Below is a graph comparing the top three categories of complaints against BellSouth since 1996.

BellSouth Complaint Analysis

1996 - 1998

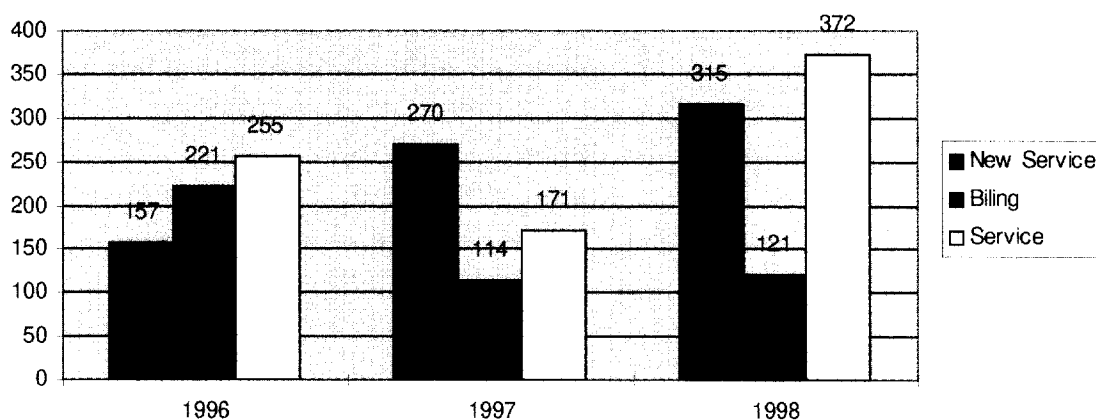


Table 20

Consumer complaints registered with the TRA against BellSouth regarding quality of service and delayed installation of new service show an upward trend since 1996. As stated earlier, BellSouth has proposed a plan, including the hiring of new staff, to address this problem. The TRA will be reviewing the progress of BellSouth's plan to determine if action is warranted.

F. Minimum Quality of Service Performance Standards

The Tennessee Regulatory Authority has rules specifying minimum quality of service standards for local telephone companies. Local telephone companies submit quarterly reports to the TRA reflecting their compliance with the minimum standards. The minimum standards are measured in terms of objective standards and surveillance standards. Companies that fail to meet the surveillance level may be subject to enforcement action by the TRA to correct the problems. The unit of analysis in the reporting is by telephone central office. This reporting disaggregation by central office permits the tracking of quality of service to the community level. Below is a description of the service standards for local telephone companies:

- **Installation of Service:** Requires, depending upon the size of the telephone exchange, that a certain percentage of service requests be completed within five working days.
- **Utility Commitment Date:** Requires a telephone company to meet 90% of its customer commitments to provide service by a date certain.
- **Customer Trouble Report:** Requires telephone companies to not exceed a certain percentage of service trouble reports per 100 access lines.
- **Call Completion:** Requires telephone companies to complete at least 97% of local dialed telephone calls.
- **Directory Assistance Call Completion:** Requires 85% of directory assistance calls answered within 10 seconds.

As indicated previously, the three (3) largest local telephone companies, BellSouth, Sprint/United and Citizens, have been granted price regulation pursuant to T.C.A. § 65-5-209. Since these three (3) companies provide service to the bulk of telephone access lines (approximately 89%) to Tennesseans, the analysis of minimum service standard performance will focus on these companies.

Sprint/United

Sprint/United is the second largest local telephone company in Tennessee and provides service in upper East Tennessee. Sprint/United met the TRA's performance standards in both 1997 and 1998. A total of 1,613 service performance observations for both years to date (months x exchanges by service category) were reviewed and Sprint/United failed to meet the TRA service performance objective in 8 of these observations. Sprint/United met the TRA's service performance objective standard 99.5% of the time during the 1997 and 1998 periods. The 1997 and 1998 data reflects a continued level trend in Sprint/United's service performance measurements since 1996.

Citizens Telephone Company

Citizens Telephone Company ("Citizens") also experienced little difficulty in meeting the TRA's service quality standards during the 1997 and 1998 period. A total of

1,413 observations were reviewed to verify Citizens' compliance with the TRA's service performance standards for both years. Citizens failed to meet the standards in 22 observations for this period. Citizens met the TRA's service performance objective standard 98.4% of the time during the years 1997 and 1998. Citizens achieved a 100% compliance with the TRA's Minimum Service Standards during 1997.

BellSouth

BellSouth's compliance with the TRA's service performance standards was also satisfactory during the years 1997 and 1998. The total 1997 and 1998 observations evaluated for BellSouth was 9,629. BellSouth failed to meet the TRA's service performance objective 179 times for both years, which results in 98.1% compliance. It should be noted that all of BellSouth's failures to meet the objective performance levels occurred in exchanges with less than 14,000 lines, or in the more rural exchanges of Tennessee.

IX. TELEPHONE ASSISTANCE PROGRAMS

A. Lifeline

The Tennessee Lifeline program was implemented in January of 1992, as a strategy to assure that all Tennesseans can afford basic telephone service. This program is available to all qualified Tennesseans and can result in reducing the monthly cost of local telephone service. In order to qualify, a person must be receiving government assistance or have an income below a certain level. A person receiving Lifeline service can enjoy minimum monthly savings of \$3.50 up to a maximum of \$13.05 for local service.

The Federal Communication Commission's ("FCC") Universal Service Order (May 1997) required the offering of this program by all telecommunications entities. This order also revamped the state offerings of Lifeline with increased discounts to qualifying states and more choice of service offerings to subscribers. Part of the change in the federal revisions of Lifeline included an increase in the amount of federal support contributed to the cost of the Program. As of June 1, 1998, 21,456 Tennesseans participated in the Lifeline Program. Annualized savings to participants are approximately \$2,700,000.⁷

The TRA has continued its support of Lifeline by maintaining the level of state support for the program. As a result of federal and state cooperation, qualified Tennesseans have the opportunity to obtain the maximum reduction in their telephone bills. This program can help ensure that all Tennesseans, regardless of income, have the opportunity to have access to telephone service.

B. Link-Up

In 1989, the Link-up Tennessee Program was implemented to assist low-income Tennesseans with the cost of installation charges for new telephone service. Link-up will pay half of the installation for telephone service, to a maximum of \$30 dollars. Tennesseans may qualify for this program if they presently receive the benefit of Food

⁷ This number reflects the savings of \$10.50 per month for the 21,456 lifeline customers times 12 months.

Stamps, Temporary Assistance to Needy Families (formerly known as AFDC), Supplemental Security Income and Medicaid. If the individual does not receive the benefit of one of these programs, they can still qualify if their household's gross monthly income is at or below 125% of the federal poverty guidelines.

CHAPTER NO. 408

SENATE BILL NO. 891

By Rochelle, Henry, Atchley, Rice, Hamilton

Substituted for: House Bill No. 695

By Bragg, Purcell, Jackson, Robinson, Napier, Bell, Wood, Davidson, Pinion, McAfee, Ford,
Byrd

AN ACT To amend Tennessee Code Annotated, Title 65, Chapter 4, Parts 1 and 2 and Title 65, Chapter 5, Part 2, relative to the regulation of telecommunications service providers by the Public Service Commission.

WHEREAS, It is in the public interest of Tennessee consumers to permit competition in the telecommunications services market; and

WHEREAS, Competition among providers should be made fair by requiring that all regulation be applied impartially and without discrimination to each; and

WHEREAS, Just and reasonable rates can be assured without use of cumbersome rate base-rate of return methods; and

WHEREAS, Universally affordable basic telephone service should be preserved; now, therefore,

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF TENNESSEE:

SECTION 1. Tennessee Code Annotated, Title 65, Chapter 4, is amended by adding the following as a new appropriately designated section:

Section 65-4-_____. Declaration of Telecommunications Services Policy. The General Assembly declares that the policy of this state is to foster the development of an efficient, technologically advanced, statewide system of telecommunications services by permitting competition in all telecommunications services markets, and by permitting alternative forms of regulation for telecommunications services and telecommunications services providers. To that end, the regulation of telecommunications services and telecommunications services providers shall protect the interests of consumers without unreasonable prejudice or disadvantage to any telecommunications services provider; universal service shall be maintained; and, rates charged to residential customers for essential telecommunications services shall remain affordable.

SECTION 2. Tennessee Code Annotated, Section 65-4-101, is amended by adding the words and punctuation "telecommunications services," between the comma following the word "telegraph" and the words "or any other like system."

SECTION 3. Tennessee Code Annotated, Section 65-4-101, is amended by adding the following new language as subsections (c), (d), (e), (f), (g), and (h):

(c) "Telecommunications Service Provider" means any Incumbent Local Exchange Telephone Company or certificated individual or entity, or individual or entity operating pursuant to the approval by the commission of a franchise within Section 6 of this act, authorized by law to provide, and offering or providing for hire, any telecommunications service, telephone service, telegraph service, paging service, or communications service similar to such services unless otherwise exempted from this definition by state or federal law.

(d) "Incumbent Local Exchange Telephone Company" means a public utility offering and providing Basic Local Exchange Telephone Service as defined by Section 65-5-208 pursuant to tariffs approved by the Commission prior to the effective date of this act.

(e) "Competing Telecommunications Service Provider" means any individual or entity that offers or provides any two-way communications service, telephone service, telegraph service, paging service, or communications service similar to such services and is certificated as a provider of such services after the effective date of this act unless otherwise exempted from this definition by state or federal law.

(f) "Interconnection Services" means telecommunications services, including intrastate switched access service, that allow a Telecommunications Service Provider to interconnect with the networks of all other Telecommunications Service Providers.

(g) "Current Authorized Fair Rate of Return" means:

(1) for an Incumbent Local Exchange Telephone Company operating pursuant to a regulatory reform plan ordered by the Commission under TPSC Rule 1220-4-2-.55, any return within the range contemplated by Section 1220-4-2-.55 (1)(c)(1) or 1220-4-2-.55 (d);

(2) for any other Incumbent Local Exchange Telephone Company, the rate of return on rate base most recently used by the Commission in an order evaluating its rates.

(h) "Gross Domestic Product-Price Index (GDP-PI)" used to determine limits on rate changes means the final estimate of the Chain-Weighted Gross Domestic Product-Price Index as prepared by the U.S. Department of Commerce and published in the Survey of Current Business, or its successor.

SECTION 4. Tennessee Code Annotated, Title 65, Chapter 5, Part 2, is amended by adding the following new language:

Section 65-5-207. Universal Service.

(a) Universal service, consisting of residential Basic Local Exchange Telephone Service at affordable rates and carrier-of-last-resort obligations must be maintained after the local telecommunications markets are opened to competition. In order to ensure the availability of affordable residential Basic Local Exchange Telephone Service, the Commission shall formulate policies, promulgate rules and issue orders which require all Telecommunications Service Providers to contribute to the support of universal service.

(b) The Commission shall, within thirty (30) days of the effective date of this act, initiate a generic contested case proceeding to determine the cost of providing universal service, determine all current sources of support for universal service and their associated amounts, identify and assess alternative universal service support mechanisms, and determine the need and timetable for modifying current universal service support mechanisms and implementing alternative universal service support mechanisms. The Commission shall issue its decision in the universal service proceeding prior to January 1, 1996.

(c) The Commission shall create an alternative universal service support mechanism that replaces current sources of universal service support only if it determines that the alternative will preserve universal service, protect consumer welfare, be fair to all Telecommunications Service Providers, and prevent the unwarranted subsidization of any Telecommunications Service Provider's rates by consumers or by another Telecommunications Service Provider. To accomplish these objectives, the Commission, if it creates or subsequently modifies an alternative universal service support mechanism, shall:

(1) restrict recovery from the mechanism by any Telecommunications Service Provider to an amount equal to the support necessary to provide universal service;

(2) consider provision of universal service by Incumbent Local Exchange Telephone Companies and by other Telecommunications Service Providers;

(3) order only such contributions to the universal service support mechanism as are necessary to support universal service and fund administration of the mechanism;

(4) administer the universal service support mechanism in a competitively neutral manner, and in accordance with established Commission rules and federal statutes;

(5) determine the financial effect on each universal service provider caused by the creation or a modification of the universal service support mechanism, and rebalance the effect through a one-time adjustment of equal amount to the rates of that provider;

(6) when ordering a modification, include changes in the cost of providing universal service in the rebalancing required by subsection (5);

(7) when performing its duties under subsections (5) and (6), order no increase in the rates for any Interconnection Services; and

(8) consider, at a minimum:

(i) the amount by which the embedded cost of providing residential Basic Local Exchange Telephone Service exceeds the revenue received from the service, including the cost of the carrier-of-last-resort obligation, for both high- and low-density service areas;

(ii) the extent to which rates for residential Basic Local Exchange Telephone Service should be required to meet the standards of Section 65-5-208(c);

(iii) intrastate access rates and the appropriateness of such rates as a significant source of universal service support.

(d) The commission shall monitor the continued functioning of universal service mechanisms and shall conduct investigations, issue show cause orders, entertain petitions or complaints, or adopt rules in order to assure that the universal service mechanism is modified and enforced in accordance with the criteria set forth in this section.

(e) Nothing in this section shall be construed to require the commission to raise residential Basic Local Exchange Telephone Service rates.

SECTION 5. Tennessee Code Annotated, Section 65-4-203, is amended by adding the

(c) The provisions of this Section shall not apply to Telecommunications Service Providers.

SECTION 6. Tennessee Code Annotated, Section 65-4-207, is amended by designating the existing language as subsection (a) and by adding the following new subsection (b):

(b) The provisions of this section shall not apply to Telecommunications Service Providers; provided, however, this section shall continue to apply with respect to any ordinance adopted, and any franchise granted pursuant to such an ordinance, prior to the effective date of this act.

SECTION 7. Tennessee Code Annotated, Section 65-4-201, is amended by designating the existing language as subsection (a) and by adding new subsections (b), (c) and (d) as follows:

(b) Except as exempted by provisions of state or federal law, no individual or entity shall offer or provide any individual or group of telecommunications services, or extend its territorial areas of operations without first obtaining from the Commission a certificate of convenience and necessity for such service or territory; provided, however, that no Telecommunications Services Provider offering and providing a Telecommunications Service under the authority of the Commission on the effective date of this act shall be required to obtain additional authority in order to continue to offer and provide such Telecommunications Services as it offers and provides as of such effective date.

(c) After notice to the Incumbent Local Exchange Telephone Company and other interested parties and following a hearing, the Commission shall grant a certificate of convenience and necessity to a Competing Telecommunications Service Provider if after examining the evidence presented, the Commission finds:

(i) The applicant has demonstrated that it will adhere to all applicable Commission policies, rules and orders; and

(ii) The applicant possesses sufficient managerial, financial and technical abilities to provide the applied for services.

A Commission order, including appropriate findings of fact and conclusions of law, denying or approving, with or without modification, an application for certification of a Competing Telecommunications Service Provider shall be entered no more than sixty (60) days from the filing of the application.

(d) Subsection (c) shall not be applicable to areas served by an Incumbent Local Exchange Telephone Company with fewer than 100,000 total access lines in this state unless such company voluntarily enters into an interconnection agreement with a Competing Telecommunications Service Provider or unless such Incumbent Local Exchange Telephone Company applies for a certificate to provide telecommunications services in an area outside its service area existing on the effective date of this act.

SECTION 8. Tennessee Code Annotated, Title 65, Chapter 4, is amended by adding the following as a new appropriately designated section:

Section 65-4-_____. Administrative Rules.

(a) All Telecommunications Services Providers shall provide non-discriminatory interconnection to their public networks under reasonable terms and conditions; and all Telecommunications Services Providers shall, to the extent that it is technically and financially feasible, be provided desired features, functions and services promptly, and on an unbundled and non-discriminatory basis from all other Telecommunications

(b) Prior to January 1, 1996, the Commission shall, at a minimum, promulgate rules and issue such orders as necessary to implement the requirements of subsection (a) and to provide for unbundling of service elements and functions, terms for resale, interLATA presubscription, number portability, and packaging of a Basic Local Exchange Telephone Service or unbundled features or functions with services of other providers.

These rules shall also ensure that all Telecommunications Services Providers who provide Basic Local Exchange Telephone Service or its equivalent provide each customer a basic White Pages directory listing, provide access to 911 Emergency Services, provide free blocking service for 900/976 type services, provide access to Telecommunications Relay Services, provide Lifeline and Link-Up Tennessee services to qualifying citizens of the state and provide educational discounts existing on the effective date of this act.

(c) The granting of applications for certificates of convenience and necessity to Competing Telecommunications Service Providers or the adoption of a price regulation plan for Incumbent Local Exchange Telephone Companies shall not be dependent upon the promulgation of these rules.

SECTION 9. Tennessee Code Annotated, Title 65, Chapter 5, Part 2, is amended by adding the following new language as:

Section 65-5-208. Competitive Rules.

(a) Services of Incumbent Local Exchange Telephone Companies who apply for price regulation under Section 65-5-209 shall be classified as follows:

1. "Basic Local Exchange Telephone Services" are telecommunications services which are comprised of an access line, dial tone, touch-tone and usage provided to the premises for the provision of two way switched voice or data transmission over voice grade facilities of residential customers or business customers within a local calling area, Lifeline, Link-Up Tennessee, 911 Emergency Services and educational discounts existing on the effective date of this act or other services required by state or federal statute. These services shall, at a minimum, be provided at the same level of quality as is being provided on the effective date of this act. Rates for these services shall include both recurring and nonrecurring charges.

2. "Non-Basic Services" are telecommunications services which are not defined as Basic Local Exchange Telephone Services and are not exempted under subsection (b). Rates for these services shall include both recurring and nonrecurring charges.

(b) The Commission, after notice and opportunity for hearing, may find that the public interest and the policies set forth herein are served by exempting a service or group of services from all or a portion of the requirements of this part. Upon making such a finding, the Commission may exempt Telecommunications Service Providers from such requirements as appropriate. The Commission shall in any event exempt a telecommunications service for which existing and potential competition is an effective regulator of the price of those services.

(c) Effective January 1, 1996, an Incumbent Local Exchange Telephone Company shall adhere to a price floor for its competitive services subject to such determination as the Commission shall make pursuant to Section 65-5-207. The price floor shall equal the Incumbent Local Exchange Telephone Company's tariffed rates for essential elements utilized by Competing Telecommunications Service Providers plus the total long-run incremental cost of the competitive elements of the service. When shown to be in the public interest, the Commission shall exempt a service or group of

or affiliated entities, predatory pricing, price squeezing, price discrimination, tying arrangements or other anti-competitive practices.

(d) The maximum rate for any new Non-Basic Service first offered after the effective date of this act shall not exceed the stand alone cost of the service.

SECTION 10. Tennessee Code Annotated, Title 65, Chapter 5, Part 2, is amended by adding the following new language as:

Section 65-5-209. Price Regulation Plan.

(a) Rates for telecommunications services are just and reasonable when they are determined to be affordable as set forth in this Section. Using the procedures established in this section, the Commission shall ensure that rates for all Basic Local Exchange Telephone Services and Non-Basic Services are affordable on the effective date of price regulation for each Incumbent Local Exchange Telephone Company.

(b) An Incumbent Local Exchange Telephone Company shall, upon approval of its application under subsection (c), be empowered to, and shall charge and collect only such rates that are less than or equal to the maximum permitted by this section and subject to the safeguards in Section 65-5-208 (c) and (d) and the non-discrimination provisions of this Title.

(c) The Commission shall enter an order within ninety (90) days of the application of an Incumbent Local Exchange Telephone Company implementing a price regulation plan for such company. With the implementation of a price regulation plan, the rates existing on the effective date of this act for all Basic Local Exchange Telephone Services and Non-Basic Services as defined in Section 65-5-208 are deemed affordable if the Incumbent Local Exchange Telephone Company's earned rate of return on its most recent TPSC 3.01 report as audited by the Commission staff pursuant to subsection (j) is equal to or less than the Company's Current Authorized Fair Rate of Return existing at the time of the Company's application. If the Incumbent Local Exchange Telephone Company's earned rate of return on its most recent TPSC 3.01 report as audited by the Commission staff pursuant to subsection (j) is greater than the Company's Current Authorized Fair Rate of Return, the Commission shall initiate a contested, evidentiary proceeding to establish the initial rates on which the price regulation plan is based. The Commission shall initiate such a rate-setting proceeding to determine a fair rate of return on the Company's rate base using the actual intrastate operating revenues, expenses, rate base and capital structure from the Company's most recent TPSC 3.01 report as audited by the Commission staff pursuant to subsection (j). If the Incumbent Local Exchange Telephone Company's earned rate of return is less than its Current Authorized Fair Rate of Return, the Company may request the Commission to initiate a contested, evidentiary proceeding to establish the initial rates upon which the price regulation plan is based. Upon request by the Incumbent Local Exchange Telephone Company, the Commission shall initiate such a contested, evidentiary proceeding using the same rate-setting procedures described above. Rates established pursuant to the above process shall be the initial rates on which a price regulation plan is based, subject to such further adjustment as may be made by the Commission pursuant to Section 65-5-207.

(d) If not resolved by agreement, the Commission shall, on petition of the Competing Telecommunications Services Provider, hold a contested case proceeding within thirty (30) days to establish initial rates for new interconnection services provided by an Incumbent Local Exchange Telephone Company subsequent to the effective date of this act, which rates shall be set in accordance with the provisions set forth in this act. The Commission shall issue a final order within twenty (20) days of the proceeding.

(e) A price regulation plan shall maintain affordable Basic and Non-Basic rates by

GDP-PI from the preceding year minus two (2) percentage points. An Incumbent Local Exchange Telephone Company may adjust its rates for Basic Local Exchange Telephone Services or Non-Basic Services only so long as its aggregate revenues for Basic Local Exchange Telephone Services or Non-Basic Services generated by such changes do not exceed the aggregate revenues generated by the maximum rates permitted by the price regulation plan.

(f) Notwithstanding the annual adjustments permitted in subsection (e), the initial Basic Local Exchange Telephone Service rates of an Incumbent Local Exchange Telephone Company subject to price regulation shall not increase for a period of four (4) years from the date the Incumbent Local Exchange Telephone Company becomes subject to such regulation. At the expiration of the four (4) year period, an Incumbent Local Exchange Telephone Company shall be permitted to adjust annually its rates for Basic Local Exchange Telephone Services in accordance with the method set forth in subsection (e) provided that in no event shall the rate for residential Basic Local Exchange Telephone Service be increased in any one (1) year by more than the percentage change in inflation for the United States using the Gross Domestic Product-Price Index (GDP-PI) from the preceding year as the measure of inflation.

(g) Notwithstanding any other provision of this act, a price regulation plan shall permit a maximum annual adjustment in the rates for Interconnection Services that is capped at the lesser of one-half (1/2) the percentage change in inflation for the United States using the Gross Domestic Product-Price Index (GDP-PI) from the preceding year as the measure of inflation, or the GDP-PI from the preceding year minus two (2) percentage points. An Incumbent Local Exchange Telephone Company may adjust its rates for Interconnection Services only so long as its aggregate revenues generated by such changes do not exceed the aggregate revenues generated by the maximum rates permitted by this subsection, provided that each new rate must comply with the requirements of Section 65-5-208 and the non-discrimination provisions of this Title. Upon filing by a Competing Telecommunications Service Provider of a complaint, such rate adjustment shall become subject to Commission review of the adjustment's compliance with the provisions of this act and rules promulgated under this act. The Commission shall stay the adjustment of rates and enter a final order approving, modifying or rejecting such adjustment within thirty (30) days of the complaint.

(h) Incumbent Local Exchange Telephone Companies subject to price regulation may set rates for Non-Basic Services as the company deems appropriate, subject to the limitations set forth in subsections (e) and (g), the non-discrimination provisions of this Title, any rules or orders issued by the Commission pursuant to Section 65-5-208(c) and upon prior notice to affected customers. Rates for call waiting service provided by an Incumbent Local Exchange Telephone Company subject to price regulation shall not exceed, for a period of four (4) years from the date the company becomes subject to such regulation, the maximum rate in effect in the state for such service on the effective date of this act.

(i) Incumbent Local Exchange Telephone Companies subject to price regulation shall not be required to seek regulatory approval of their depreciation rates or schedules.

(j) For any Incumbent Local Exchange Telephone Company electing price regulation under Section 65-5-209(c), the Commission shall conduct an audit to assure that the TPSC 3.01 Report accurately reflects, in all material respects, the Incumbent Local Exchange Telephone Company's achieved results in accordance with Generally Accepted Accounting Principles as adopted in Part 32 of the Uniform System of Accounts, and the ratemaking adjustments to operating revenues, expenses and rate base used in the Commission's most recent order applicable to the Incumbent Local Exchange Telephone Company. Nothing herein is to be construed to diminish the audit powers of the Commission.

(k) Incumbent Local Exchange Telephone Companies subject to price regulation shall maintain their commitment to the FYI Tennessee Master Plan to the completion of

the funded requirements with any alterations to the plan to be approved by the Commission.

SECTION 11. Tennessee Code Annotated, Title 65, Chapter 5, Part 2, is amended by adding the following new language as:

Section 65-5-210. Commission Jurisdiction.

(a) In addition to any other jurisdiction conferred, the Commission shall have the original jurisdiction to investigate, hear and enter appropriate orders to resolve all contested issues of fact or law arising as a result of the application of this act.

(b) The Consumer Advocate shall retain all powers with respect to this act as is provided in Tennessee Code Annotated, Section 65-4-118, or any future legislation.

SECTION 12. Nothing in this act shall be construed as removing the powers of the Commission pursuant to Tennessee Code Annotated, Section 65-5-202.

SECTION 13. Nothing in this Act shall affect the authority and duty of the Commission to complete any investigation pending at the time this act becomes effective.

SECTION 14. Nothing in this act shall be construed to affect the assessment for ad valorem taxation of property used to provide telecommunications services, and to that end it is declared that the fifty-five percent (55%) level of assessments shall remain applicable to property used in whole or in part to provide telecommunications services other than cellular telephone services, radio common carrier services, or long distance telephone services.

SECTION 15. The General Assembly shall evaluate the implementation of the provisions of this act every two (2) years for not less than the next six (6) years by requiring the submission of a report prepared by the Commission consisting of the following information:

- (a) The compliance of market participants with the provisions of this act;
- (b) The status of universal service in Tennessee;
- (c) The availability of service capabilities and service offerings subdivided by facilities-based and non-facilities-based, for each Telecommunications Services Provider;
- (d) The number of customers, access lines served, and revenues, subdivided by residential and business, for each Telecommunications Services Provider;
- (e) The impact of federal telecommunications initiatives;
- (f) The degree of technological change in the marketplace;
- (g) The technical compatibility between providers;
- (h) The service performance of providers; and,
- (i) Any other information the Commission considers necessary to proper oversight and evaluation.

SECTION 16. Each Telecommunications Service Provider shall file with the commission a small and minority owned telecommunications business participation plan within sixty (60) days of the effective date of this act. Competing Telecommunications Service Providers shall file such plan with the Commission with their application for a certificate. Such plan shall contain such entity's plan for purchasing goods and services from small and minority telecommunications businesses and information on programs, if any, to provide technical assistance to such businesses. All providers shall update plans filed with the commission annually. For purposes of this act, the term "minority business" means a business which is solely owned, or at least fifty-one percent (51%) of the assets or outstanding stock of which is

owned, by an individual who personally manages and controls the daily operations of such business, and who is impeded from normal entry into the economic mainstream because of race, religion, sex or national origin and such business has annual gross receipts of less than four million dollars (\$4,000,000). For purposes of this act, the term "small business" means a business with annual gross receipts of less than four million dollars (\$4,000,000).

SECTION 17. (a) The Department of Economic and Community Development, with assistance from the Comptroller of the Treasury relative to loan guarantees, shall develop by rule an assistance program for small and minority telecommunications businesses no later than January 1, 1996. Such plan shall require Telecommunications Service Providers and Competing Telecommunications Service Providers to contribute a total of two million dollars (\$2,000,000) each year for five (5) years for a total amount of ten million dollars (\$10,000,000) to fund the small and minority telecommunications business assistance program. The Commission shall by rule determine the contribution to be made each year by each Telecommunications Service Provider and each Competing Telecommunications Service Provider to such program. The contribution of each such entity shall be determined in accordance with the process used to determine universal service support contributions in accordance with the provisions of Section 4(a). The small and minority telecommunications business assistance program shall provide for loan guarantees, technical assistance and services, and consulting and education services. The Department of Economic and Community Development shall administer the small and minority telecommunications business assistance program except that the Comptroller of the Treasury shall administer any loan guarantees provided pursuant to such program. It is the legislative intent that such program be designed with consideration of fair distribution of program assistance among the geographic areas of the state with no more than forty percent (40%) of program assistance to be awarded in any grand division and fair distribution of program assistance among small and minority telecommunications businesses.

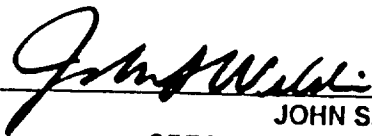
(b) The Department of Economic and Community Development shall give an interim report on the development of the small and minority telecommunications business assistance program to the House and Senate State and Local Government Committees and to the House Commerce and Senate Commerce, Labor and Agriculture Committees no later than September 1, 1995. Such committees shall report its comments and recommendations on such report to the department within thirty (30) days of receiving such report.

(c) The small and minority telecommunications business assistance program developed by the Department of Economic and Community Development shall take effect on March 1, 1996, unless modified or repealed by legislation enacted prior to such date.

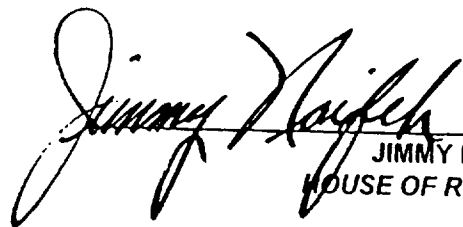
(d) There is established a general fund reserve to be allocated in accordance with the small and minority telecommunications business assistance program created by this act which shall be known as the small and minority telecommunications business assistance program fund. Moneys from the fund may be expended in accordance with such program. Any moneys deposited in the fund shall remain in the reserve until expended for purposes consistent with such program and shall not revert to the general fund on any June 30. Any interest earned by deposits in the reserve shall not revert to the general fund on any June 30 but shall remain available for expenditure in subsequent fiscal years.

SECTION 18. If any provision of this act or the application thereof to any person or circumstance is held invalid, such invalidity shall not affect other provisions or applications of the act which can be given effect without the invalid provision or application, and to that end the provisions of this act are declared to be severable.

SECTION 19. This act shall take effect upon becoming a law, the public welfare requiring it.

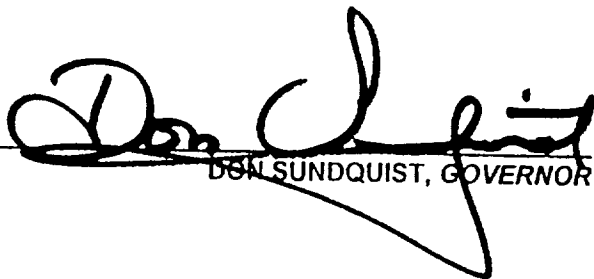


JOHN S. WILDER
SPEAKER OF THE SENATE



JIMMY NAIFEH, SPEAKER
HOUSE OF REPRESENTATIVES

APPROVED this 6 day of June 1995



DON SUNDQUIST, GOVERNOR

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

December 9, 1998

IN RE:

**APPLICATION OF BELL SOUTH
TELECOMMUNICATIONS, INC.
FOR A PRICE-REGULATION
PLAN**

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DOCKET NO. 95-02614

**ORDER APPROVING BELL SOUTH TELECOMMUNICATIONS, INC.'S
APPLICATION FOR PRICE REGULATION PLAN**

This matter came before the Tennessee Regulatory Authority ("Authority") during a special Authority Conference held on October 27, 1998, for consideration of BellSouth Telecommunications, Inc.'s ("BellSouth") application for a price regulation plan. In *BellSouth Telecommunications, Inc. v. Greer*, 972 S.W.2d 663 (Tenn. Ct. App. 1997), appeal denied, Case No. 01A01-9601-BC-00008 (June 15, 1998), the Tennessee Court of Appeals remanded this case to the Authority "with directions to approve BellSouth's application for a price regulation plan" and to conduct "further proceedings consistent with the requirements of Tenn. Code Ann. § 65-5-209."

On January 23, 1996, the Tennessee Public Service Commission entered an order, pursuant to Tenn. Code Ann. § 65-5-209, implementing BellSouth's price regulation plan and requiring that BellSouth reduce its rates by approximately 56.3 million dollars. On October 1, 1997, in a lengthy opinion, the Court of Appeals for the Middle Section of Tennessee vacated the order of the Public Service Commission and remanded the matter to the Tennessee Regulatory Authority to approve

BellSouth's price regulation application. The Court of Appeals issued another opinion on November 19, 1997, denying motions for rehearing. On January 20, 1998, the Authority and the Consumer Advocate Division Office of the Attorney General ("Consumer Advocate") filed in the Tennessee Supreme Court an application for permission to appeal the Court of Appeals' decision. The Supreme Court denied that application on June 15, 1998.

On June 29, 1998, the Court of Appeals issued its mandate to the Authority to implement the Court's decisions of October 1, 1997 and November 19, 1997. On July 10, 1998, BellSouth filed a Motion to Implement Appellate Court's Mandate ("Motion to Implement"). Thereafter, this matter was considered at the Authority Conference on July 21, 1998, for the purpose of requesting interested parties to file responses to BellSouth's motion.¹ Responses were submitted to the Authority by the following parties: Consumer Advocate Division, Office of the Attorney General ("Consumer Advocate"); MCI Communications, Corp. ("MCI"); AT&T Communications of the South Central States, Inc. ("AT&T") and American Association of Retired Persons ("AARP").

Pending before the Authority at the October 27, 1998, Special Authority Conference were: (1) BellSouth's Motion to Implement Appellate Court's Mandate; and (2) a "Motion to Begin Afresh or Alternatively a Complaint or Petition," as amended, filed by the Consumer Advocate.

I. FINDINGS OF FACT AND CONCLUSIONS OF LAW

A. Procedural History

On June 20, 1995, BellSouth filed an application with the Tennessee Public Service Commission ("Commission") to operate under price regulation pursuant to Tenn. Code Ann. § 65-

¹ At the July 21, 1998, Authority conference the Directors voted to receive in Docket No. 95-02614 written responses from parties to be filed within fourteen (14) days. The American Association of Retired Persons ("AARP") subsequently requested a one day extension for filing its response which was granted by the Authority at its August 18, 1998, Conference.

5-209. The application requested that the Commission enter an order approving a price regulation plan for BellSouth effective October 1, 1995, with the initial rates being those in effect on June 6, 1995.

On September 15, 1995, the Commission Staff issued its Report of BellSouth's Form 3.01 report for the twelve months ended March 31, 1995, which the Commission had concluded was the appropriate 3.01 report to audit under Tenn. Code Ann. § 65-5-209(j). The Report stated:

Except for three corrections made by the Staff, the rate of return reported on the March, 1995 TPSC 3.01 Report is accurately taken from the Company's books and records, and reflects Commission ordered ratemaking adjustments. Nothing came to our attention to indicate that the Company had not complied with Generally Accepted Accounting Principles or USOA, Part 32, accounting. The corrected rate of return for the twelve months ended March 1995 as taken from the books is 10.30%.

The audited return of 10.30% was below BellSouth's then authorized return of 10.65% - 11.85%.

The Report also reflected that the Commission Staff adjusted BellSouth's corrected rate-of-return for out of period adjustments, abnormal or unusual financial occurrences, and known changes occurring through March 31, 1995, which resulted in an "adjusted" return of 12.74%. Because this "adjusted" return was above BellSouth's authorized rate of return, the Staff recommended that the Commission conduct a contested case hearing to set BellSouth's initial rates for price regulation purposes.

On September 20, 1995, the Commission accepted the Staff's audit report and subsequently convened a contested case proceeding for the purpose of establishing BellSouth's rates prior to entering price regulation. On January 23, 1996, the Commission entered its order implementing a price regulation plan for BellSouth, finding that BellSouth's rate of return should be 10.35% and

requiring that BellSouth file tariffs to reduce its rates by \$56.285 million dollars (\$56,285,000), consistent with the rate design established by the Commission.²

On February 14, 1996, BellSouth filed a petition for review with the Tennessee Court of Appeals. BellSouth contended that the Commission's "adjustments" to BellSouth's earned rate of return were unlawful and that its initial rates for the purposes of price regulation should have been those rates existing as of June 6, 1995, because BellSouth's earned rate of return on its most recent Form 3.01 Report as audited by the Commission Staff was less than BellSouth's authorized rate of return.³

On October 1, 1997, the Court of Appeals entered its order and opinion vacating the Commission's January 23, 1996, Order and all earlier entered orders. The Court held that Tenn. Code Ann. § 65-5-209(j) empowered the Commission to audit BellSouth's Form 3.01 Report for the following purposes: (1) to verify that the information on the report accurately reflects the information in BellSouth's books and records; (2) to verify that the report was prepared consistently with generally accepted accounting principles; and (3) to verify that BellSouth's calculations reflected the Commission's previously issued orders. 972 S.W.2d at 680. The Court stated that "[t]he Commission's authority to adjust the figures on the Form PSC-3.01 Report is limited to correcting errors with regard to these three categories." *Id.*

² The Commission's Order of January 23, 1996, reflects a two to one (2-to-1) decision, in which Commissioner Sara Kyle and Chairman Keith Bissell supported the above-mentioned reduction in BellSouth's rates. Commissioner Steve Hewlett concurred with the overall rate reduction, however, he did not concur with the rate design adopted by the majority.

³ AT&T also filed a petition for review of the Commission's order, alleging that the Commission had failed to follow the proper standards and procedures in implementing a price regulation plan for BellSouth. According to AT&T, before an application for price regulation can be approved, the tariff and rate for each service offered by an incumbent must be reviewed to determine whether they are just and reasonable as well as nondiscriminatory. The Court rejected this position and specifically stated that "the Commission had already determined that these rates and tariffs were just and reasonable and nondiscriminatory, it is not required to make the determination again absent some specific reason to do so." See 972 S.W.2d at 682.

The Court of Appeals concluded that the Commission exceeded its authority by adjusting the earned rate of return reflected on BellSouth's Form 3.01 Report "to compensate for out of period items, abnormal or unusual expenses, and known changes." According to the Court:

[The Commission] had already concurred with its staff's conclusion that the rate of return on BellSouth's corrected Form PSC-3.01 report was 10.30%. Since this rate did not exceed BellSouth's currently authorized rate of return of between 10.65 and 11.85%, the Commission should have found that BellSouth's existing rates were affordable under Tenn. Code Ann. § 65-5-209(a) and should have approved BellSouth's application for a price regulation plan based on BellSouth's rates existing on June 6, 1995 as required by Tenn. Code Ann. § 65-5-209(c).

Id. In addition to vacating the Commission's orders, the Court of Appeals remanded the case to the Authority "with directions to approve BellSouth's application for a price regulation plan." *Id.* at 682. The parties filed petitions for re-hearing before the Court of Appeals.

On November 19, 1997, the Court of Appeals issued an order denying the petitions for rehearing. BellSouth in its petition asked the Court of Appeals to fix the effective date of its price regulation plan as March 1, 1996. The Court noted that its "October 1, 1997 opinion settles the dispute concerning what Tenn. Code Ann. § 65-5-209 requires. Now it falls upon the Tennessee Regulatory Authority to consider BellSouth's application for a price regulation plan in accordance with Tenn. Code Ann. § 65-5-209." *Id.* at 683.

On January 20, 1998, the Authority and the Consumer Advocate filed an application for permission to appeal with the Tennessee Supreme Court. The Supreme Court denied the application on June 15, 1998, and on June 29, 1998, the Court of Appeals issued its mandate to the Authority.

B. Contentions Of The Parties

1. BellSouth

In its Motion to Implement, BellSouth urges the Authority as a matter of law to approve its application for price regulation, contending that it seeks nothing more and nothing less than what BellSouth requested in its June 20, 1995 application. BellSouth further contends that the Authority must approve its application without a new audit and hearings by noting that, had the Commission acted lawfully, BellSouth would have been operating under a price regulation plan effective October 1, 1995, with initial rates being those in effect on June 6, 1995, and that BellSouth should not be penalized for the Commission's failure to follow the law.

BellSouth supports its position by asserting that the Court of Appeals held that the Commission "should have found that BellSouth's existing rates were affordable under Tenn. Code Ann. § 605-5-209(a) and should have approved BellSouth's application for price regulation based on BellSouth's rates existing on June 6, 1995, as required by Tenn. Code Ann. § 65-5-209(c)." *Greer*, 972 S.W.2d at 680. Accordingly, BellSouth asserts that the Court of Appeals has remanded this case with explicit instructions for the Authority to approve BellSouth's application for a price regulation plan.

BellSouth also cites *Hoover, Inc. v. Metropolitan Board of Zoning Appeals for Davidson County, Tennessee*, 955 S.W.2d 52, 55 (Tenn. Ct. App. 1997), and *Getty v. Federal Savings & Loan Ins. Corp.*, 805 F.2d 1050, 1061 (D.C. Cir. 1986), for the proposition that the fundamental purpose of a remand is to place the parties and the agency in the position they would have been in had the agency not acted improperly. BellSouth further anchors its position by opining that the Authority cannot lawfully conduct further proceedings, specifically that the Authority cannot

conduct an audit of BellSouth's most recently filed Form 3.01 Report. It states that convening a proceeding to conduct such an audit would violate Tenn. Code Ann § 65-5-209 as interpreted by the Court of Appeals.

While contending that the Authority must approve its application for price regulation, BellSouth acknowledges that putting it in the same position it would have been in had the Commission not acted improperly poses certain practical difficulties. Accordingly, contingent upon the approval of its application for price regulation with an effective date of October 1, 1995, based on the rates existing on June 6, 1995, and the adoption of the price regulation methodology stipulated to in *In re: United Telephone Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423, BellSouth stated that it would not object to entry of an order which also provides that:

(1) increases in the initial rates for Basic Local Exchange Telephone Service shall not occur until August 1, 2002, consistent with Tenn. Code Ann. § 65-5-209(f);

(2) increases in the rates for Call Waiting shall not occur until August 1, 2002, consistent with Tenn. Code Ann. § 65-5-209(h);

(3) annual adjustments in basic and nonbasic rates pursuant to Tenn. Code Ann. § 65-5-209(e) shall be calculated from August 1, 1998, and the calculation of the Service Price Index for basic and nonbasic services shall be based upon service volumes for the month of August for the year of the annual filing and upon service prices in effect on August 1, 1998 or as reset by the TRA under Tenn. Code Ann. § 65-5-207; and

(4) annual adjustments in Interconnection Services pursuant to Tenn. Code Ann. § 65-5-209(g) shall be calculated from August 1, 1998.

(BellSouth's Memorandum in Support of Motion to Implement Appellate Court's Mandate, at 5).

2. Consumer Advocate Division

In its Motion to Begin Afresh, filed on July 22, 1998, the Consumer Advocate takes the position that the Authority should begin the hearing process afresh before approving BellSouth's application for a price regulation plan. The Consumer Advocate's argument shifts between what it construes the law to require the Authority to do and what it believes the Authority should do based upon the Consumer Advocate's view of sound and substantive policy in evaluating BellSouth's application at this point in time.

The salient points of the Consumer Advocate's arguments are as follows: (1) economics have changed, and BellSouth was not and is not operating pursuant to a price regulation plan causing existing rates and prior rates to be unjust and unreasonable; (2) Tenn. Code Ann. §§ 65-5-201 and 65-5-203(c) are applicable to BellSouth until it is validly regulated under another valid order and regulatory mechanism; (3) because the effective date of price regulation is linked to affordable rates, it is inappropriate to use results from administrative procedures related to a different effective date in lieu of procedures to ensure affordability at a later date; (4) the Commission Staff audit did not assure that the Form 3.01 report accurately reflected in all material respects BellSouth's achieved results in accordance with Generally Accepted Accounting Principles ("GAAP") as adopted in Part 32 of the Uniform System of Accounts, and the appropriate ratemaking adjustments;⁴ (5) the Commission Staff recognized that it had not performed audit work necessary to attest to BellSouth's compliance as is required by Tenn. Code Ann. § 65-5-209; (6) failure to start afresh would place BellSouth in an improved position and the Authority should not

⁴ In fact the CAD asserts that the procedural error began with the Tenn. Code Ann § 65-5-209 (j) audit and that the audit should begin afresh and an opportunity for a contested case on the ensuing audit should be granted. It should be noted that this prong of the CAD's attack on the audit was originally raised before the Commission, but not pursued by the CAD before the Court of Appeals.

improve BellSouth's position, citing *Getty v. Federal Savings & Loan Insurance Corporation*; (7) the Consumer Advocate asserts that it has a due process right to challenge the Commission Staff's Report, a right denied by the Commission, and that the Authority must advocate that BellSouth's 3.01 Report is in accordance with GAAP and Part 32 through witnesses subject to cross-examination; (8) that BellSouth is operating pursuant to TRA Rule 1220-4-2-55, and that BellSouth is estopped from denying the same.

3. AT&T

In asserting its position, AT&T relies upon the Court of Appeals' findings that the Commission exceeded its authority by making adjustments to BellSouth's Form 3.01 report and that the Commission should have found that BellSouth's rates were affordable and should have approved its application for a price regulation plan based on its rates existing on June 6, 1995. In so doing AT&T has alleged that BellSouth's Motion to Implement makes an unwarranted leap from what the Commission should have done to a conclusion as to what the Authority must now do. AT&T argues that the Court of Appeals' action of vacating not only the Commission's January 23, 1996, Order, but also all prior related orders with respect to BellSouth's application, is an indication that the Authority must now consider afresh BellSouth's application for a price regulation plan in accordance with Tenn. Code Ann. § 65-5-209 as construed by the Court. AT&T additionally takes the position, as does the Consumer Advocate, that any person in this proceeding, including AT&T, whose legal rights and privileges are affected by the Authority's interpretation or use of the Commission Staff audit would have the right to a contested case hearing to challenge that interpretation or use.

AT&T also argues that nothing in Tenn. Code Ann. § 65-5-209, or in any other statute or opinion of the Court, gives the Authority the power to approve, implement, or make effective a price regulation plan retroactively. Thus, according to AT&T, the Authority has no power to approve, implement, or make effective BellSouth's price regulation plan as stated in BellSouth's original application. AT&T argues that the limitation on the power of the Authority to make BellSouth's price regulation plan effective as of October 1, 1995, is not only practical, but is also imposed by law. BellSouth's Motion to Implement seeking the approval of its price regulation plan effective October 1, 1995, according to AT&T, is inconsistent with the law.

Finally, AT&T, in noting the passage of time between the Commission Staff audit and these proceedings, conclude that a report for the period ending March 31, 1995, filed in June 1995, could not be considered "most recent" for the purpose of implementing and making effective a price regulation plan in 1998.

4. American Association of Retired Persons

AARP basically argues that BellSouth's Motion to Implement should be rejected because it does not follow the procedures set forth in the Court of Appeals' October 1, 1997, opinion and its November 19, 1997, decision on rehearing. AARP asserts that: (1) the Court of Appeals did not address the question of which Form 3.01 report should be used when implementing BellSouth's price regulation plan; (2) the Authority must now exercise its own expertise and decide this issue; and (3) since the Commission's January 23, 1996, Order has been vacated, the Authority must now issue a completely new order that addresses the substance or merits of BellSouth's price regulation plan. According to AARP, BellSouth's proposal does not address the substance or merits of BellSouth's price regulation plan; rather it simply approves the rates in effect today. AARP also

contends, similar to the positions put forth by the Consumer Advocate and AT&T, that the Authority must now conduct a complete audit since the Commission Staff's audit of BellSouth's Form 3.01 report is only a partial audit.

C. Discussion

The Court of Appeals' October 1, 1997, decision and the Court's subsequent decision on November 19, 1997, denying BellSouth's motion for rehearing have become the law of this case and operate as the legal interpretation of the requirements of Tenn. Code Ann. § 65-5-209. In fact, in its decision on rehearing, the Court referred to its October 1, opinion as providing guidance to the Authority in further considering BellSouth's application. *See Greer*, 972 S.W.2d at 683. The Court's October 1, opinion, makes it clear that consideration pursuant to Section 65-5-209 requires the approval of BellSouth's application for a price regulation plan.

While all parties agree unequivocally that the Authority has been directed by the Court of Appeals to approve BellSouth's application for a price regulation plan, there is disagreement among the parties as to what manner and under what circumstances Authority approval is to be effectuated. For example, the Consumer Advocate, AT&T, and the AARP question which Form 3.01 report should be used as a basis for the approval of BellSouth's application for price regulation. These parties contend that the Authority should rely upon BellSouth's most recent Form 3.01 Report, which would necessitate a new audit. BellSouth asserts that the Authority should rely on the March 31, 1995 Form 3.01 report.

The Court of Appeals construed Tenn. Code Ann. § 65-5-209(c) as requiring "an audit of the existing telephone company's most recent Form PSC-3.01 report available when the company filed its application for a price regulation plan." 972 S.W.2d at 668, n.14. BellSouth had already

filed a Form PSC-3.01 report for the twelve months ending on March 31, 1995, when it applied for a price regulation plan. It is reasonable to conclude from the Court of Appeals' opinion that the March 31, 1995 Report "was BellSouth's most recent report" for purposes of the Section 65-5-209(j) audit. *Id.* Thus, in considering BellSouth's application for a price regulation plan, the Authority is relying upon BellSouth's Form 3.01 report for the twelve months ending on March 31, 1995. To do otherwise would, in the opinion of the Authority, be contrary to the Court's October 1, 1997, opinion.

AT&T asserts that BellSouth "amended" its June 20, 1995, application for a price regulation plan by filing its Motion to Implement which contained an offer to extend the caps on the rates for basic services and Call Waiting until 2002. Thus, according to AT&T, the most recent Form 3.01 report for purposes of the audit is at least the Form 3.01 report on file at the time BellSouth filed its Motion to Implement on July 10, 1998.

BellSouth's Motion to Implement only requested that the Authority enter an order approving the application that BellSouth filed for price regulation on June 20, 1995, including the originally requested effective date of October 1, 1995. BellSouth's statement that it would not object, under specified circumstances, to the entry of an order granting BellSouth's application and making BellSouth subject to price regulation on a going forward basis does not constitute an amendment to the price regulation application. AT&T's position fails to consider that the purpose of the remand from the Court of Appeals is to place BellSouth and the Authority in the position that they would have been in had the Commission not acted improperly. *See Hoover*, 955 S.W.2d at 55. It is clear to the Authority that in remanding this case to the Authority, with directions to approve BellSouth's application, the Court intended that the Authority consider BellSouth's pending application.

BellSouth's Motion to Implement only proposed a manner in which the Authority could move forward in a case that had "new life" breathed into it by action of the Court and did not constitute an amended price regulation application.

The Consumer Advocate, AT&T, and the AARP also object to the Authority's reliance upon the March 31, 1995, Form 3.01 report in approving BellSouth's price regulation plan, arguing that the Commission Staff audit of that report does not comport with the requirements of Tenn. Code Ann. § 65-5-209(j). For example, the Staff audit report contains a "statement of negative assurance," which does not meet the positive assurance requirements of generally accepted auditing standards and which is a prohibited expression in an auditor's report in conformity with GAAP. Furthermore, Mike Gaines, then Manager of the Commission's Telecommunications Section, testified that the Commission "simply did not have the staff or time available to do an audit necessary to issue a positive opinion that the company's accounting was in accordance with GAAP and Part 32 Accounting" and acknowledged that the Commission Staff relied upon the work of other auditors, even though the Staff "did not talk with the auditors or review the work papers related to those audits."⁵ Notwithstanding the qualifying language in the Commission Staff audit and any deficiencies in the process employed by the Staff, the audit report of BellSouth's March 31, 1995, Form 3.01 report was presented to the Commission intact and was determined by the Commission to be in compliance with Section 65-5-209(j). The Commission voted unanimously to

⁵ Whether or not the Commission Staff conducted an audit that complied with the requirements of Section 65-5-209(j), the Authority rejects the AARP's argument that the Commission Staff "may have improperly included an adjustment under the abnormal and unusual category rather than the staff corrections to [Net Operating Income] category." While there may be a question in the AARP's mind under which category this adjustment should fall, an important aspect of conducting an independent audit is to render professional judgment. Substituting a party's judgment for that of the Commission's auditors is a proposition that could result in as many different judgments as there are parties, and, in the Authority's view, goes far afield of what must be decided in approving BellSouth's application for a price regulation plan.

set BellSouth's rates based on expenses, revenues, and rate base from the Staff audit report of BellSouth's March 31, 1995, Form 3.01 report.

It should be noted that in its summary of the case's history, the Court stated that the Commission Staff concluded that BellSouth's March 31, 1995, Form 3.01 report "complied with the generally accepted accounting principles as adopted in Part 32 of the Uniform System of Accounts." 972 S.W.2d at 668. The Court of Appeals also specifically found that the Commission "concurred with its staff's conclusion that the rate of return on BellSouth's corrected Form PSC-3.01 Report was 10.30 percent." The Court concluded that "the Commission should have found that BellSouth's existing rates were affordable under Tenn. Code Ann. § 65-5-209(a), and should have approved BellSouth's application for a price regulation plan based on BellSouth's rates existing on June 6, 1995, as required by Tenn. Code Ann. § 65-5-209(c)." 972 S.W.2d at 680.

It is not clear whether the Court fully considered the meaning of a negative assurance statement, or whether it fully considered its meaning and notwithstanding such consideration, chose the language that it did. The Court's opinion does not discuss the technical definitions or the significance of the accounting principles dictated by GAAP or by Part 32 of the USOA. Nonetheless, the grammatical change the Court made to the Commission Staff's actual statement transformed the Commission Staff's technically correct statement of negative assurance to a technically incorrect positive statement of compliance. Still, however, given the Court's statement that the Commission concluded that the audit complied with GAAP as adopted in Part 32 of the USOA, it is reasonable to conclude that the testimony of witnesses in the record persuaded the Court that even if the audit contained some flaws, such flaws were not material to the result of the

finding that BellSouth's rate of return from the March 31, 1995, Form 3.01 Report was 10.3 percent.

Although the Commission Staff's audit report contained a statement of negative assurance, the Court of Appeals had before it the testimony of Mike Gaines who headed the Staff audit. Mr. Gaines testified before the Commission under cross-examination by James Harralson of BellSouth during the hearing on November 1, 1995, to the following:

Q: If stated in accordance with generally accepted accounting principles as adopted by Part 32, and in accordance with ratemaking adjustments from the August 20, 1993, order in the company's last rate case, what should the rate of return on line 29 be?

A: 10.30.

(Nov. 1, 1995 Tr., Vol. I at 89). From this response, even with the negative assurance of the audit, the Court reasonably could have concluded that the result of the audit, i.e., a finding that BellSouth's earned rate of return was 10.30%, would have been the same had the audit contained a positive opinion. Based upon the evidence in the record, the Authority concludes that the Court of Appeals found that the lack of a positive opinion was not material to the ultimate result. Furthermore, other than the improper adjustments challenged by BellSouth, none of the other parties raised an issue on appeal as to whether the audit, absent such adjustments, complied with the requirements of Section 65-5-209(j).

After carefully and painstakingly reviewing the record before it, the Court rendered a well-written and well-reasoned opinion that the Authority is bound to follow. The Authority has received this remand from the Court of Appeals with a lawful directive to approve BellSouth's application for

a price regulation plan. After reviewing the Court's opinion and the briefs of the parties, the Authority must conclude that the Court said what it meant and meant what it said.

The Consumer Advocate, AT&T, and the AARP argue eloquently, capably, and forcibly that the Authority must rehear all issues anew. In support of their position, these parties rely upon the Court of Appeals' language that its "October 1, 1997, opinion settles the dispute concerning what Tenn. Code Ann. Section 65-5-209 requires" and that "it now falls upon the Tennessee Regulatory Authority to consider BellSouth's application for a price regulation plan in accordance with Tenn. Code Ann. Section 65-5-209." 972 S.W.2d at 683. This language however, does not constitute the whole of the Court's opinion. Equally applicable with respect to this remand is that the Court, after outlining what it considered to be the Commission's errors in conducting the audit, determined that, absent the improper adjustments, the audit performed by the Commission Staff was sufficient under Section 65-5-209 to approve BellSouth's application. This is set forth in the following language of the Court's opinion:

The Commission exceeded its authority under Tenn. Code Ann. § 65-5-209(c) & (j) by adjusting the figures in BellSouth's Form PSC-3.01 report to compensate for out of period items, abnormal or unusual expenses, and known charges. It had already concurred with its staff's conclusion that the rate of return on BellSouth's corrected Form PSC-3.01 report was 10.30%. Since this rate of return did not exceed BellSouth's currently authorized rate of return of between 10.65 and 11.85%, the Commission should have found that BellSouth's existing rates were affordable under Tenn. Code Ann. § 65-5-209(a) and should have approved BellSouth's application for a price regulation plan based on BellSouth's rates existing on June 6, 1995, as required by Tenn. Code Ann. § 65-5-209(c).

972 S.W.2d at 680.

Additional language to this effect appears in the October 1, 1997, decision wherein the Court addresses AT&T's arguments concerning the procedure followed by the Commission. The Court again indicates that the audit performed by the Commission Staff, without the adjustments

challenged by BellSouth, complied with the requirements of Section 65-5-209(j) and was sufficient to support a determination that BellSouth's rates were affordable under Section 65-5-209(c) so as to require the Commission's approval of BellSouth's application. The Court stated:

AT&T also argues that the Commission did not complete its task because it failed to review each of BellSouth's rates and tariffs to determine whether they were affordable and non-discriminatory. We need not address this issue in light of our holding that the Commission should have approved BellSouth's application for a price regulation plan based on the rates in existence on June 6, 1995. Since the Commission had already determined that these rates and tariffs were just and reasonable and nondiscriminatory, it is not required to make this determination again absent some specific reason to do so.

972 S.W.2d at 681-682 (footnote omitted).

Moreover, the Court chose language in its remand which specifically relies on the action taken by the Commission and which indicates that in the Court's judgment, which judgment the Authority is now bound to enforce, the Commission Staff audit complies sufficiently with the statute such that this Authority is required to proceed to approve BellSouth's application without performing another audit. The Court closes its October 1 opinion with the following language:

In summary, we vacate the Commission's January 23, 1996 order and all related orders with regard to BellSouth's application for a price regulation plan. Since the Commission has adopted its staff's conclusion that BellSouth's rate of return reported on its Form PSC-3.01 Report for the twelve months ending March 31, 1995 is less than its current authorized rate of return, we remand the case to the Tennessee Regulatory Authority with directions to approve BellSouth's application for a price regulation plan. In light of our conclusion that the Commission did not have the Authority to adjust the actual results on BellSouth's Form PSC-3.01 Report, we need not consider the remaining issues raised by BellSouth and AT&T. These issues and all other issues raised by the parties are accordingly pretermitted.

972 S.W.2d at 682.

Finally, the Court's October 1, 1997, opinion sets forth the reasons why the adjustments to BellSouth's rate of return made by the Commission Staff were not permissible under the scope of the

audit contemplated by Section 65-5-209(j). The Court could have but did not discard the entire audit. To the contrary, by making statements such as the Commission should have approved BellSouth's application and "we remand the case to the TRA with directions to approve BellSouth's application for a price regulation plan," the plain language of the Court's opinion reveals that the court determined that the remainder of the audit is legally sound, that no further audit is necessary, and that the Authority had no discretion other than to approve BellSouth's application for price regulation plan "absent some specific reason to do so." Given the strength of the Court's acceptance of Commission Staff's audit as being 65-5-209(j) compliant, such specific reasons are not present in this case.

The Authority is unpersuaded by AT&T's contention that any person, including AT&T, whose legal rights and privileges are affected by the Authority's interpretation or use of the Commission Staff's audit has the right to a contested case hearing to challenge that interpretation or use. Equally unpersuasive is the Consumer Advocate's assertion that it has a due process right to challenge the Staff's audit report which was denied to it by the Commission. With respect to AT&T's contention, the Court of Appeals' holding that BellSouth was entitled to a hearing on the Commission Staff's audit was limited solely under the circumstances presented in this case to BellSouth. Further, both AT&T's and the CAD's arguments are inconsistent with *Consumer Advocate Division v. Bissell*, 1996 Tenn. App. LEXIS 528, *12 (Tenn. Ct. App. Aug. 28, 1996) (holding that "tariff does not violate the due process rights of the ratepayers because it raises or lowers their rates without a hearing"), and *AT&T Communications of the South Central States, Inc. v. Greer*, 1996 Tenn. App. LEXIS 776, *11 (Tenn. Ct. App. Dec. 6, 1996).

With respect to the effective date of BellSouth's price regulation plan, certain parties have raised issues of retroactivity and the amendment of BellSouth's application. AT&T states that, "Nothing in TCA Section 65-5-209 or in any other statute or in any opinion of the Court gives the TRA the power to approve, implement, or make effective the price regulation plan retroactively. Thus, the TRA has no power to approve, implement, or make effective BellSouth's price regulation plan as stated in BellSouth's original application." After reviewing the Court's opinion and the filings, a determination by this Authority that BellSouth's price regulation plan would have been effective October 1, 1995, had the Commission acted lawfully is squarely within the Authority's discretion. The Authority concludes further that BellSouth's Motion to Implement does not constitute an amendment to BellSouth's price regulation application. The fact that BellSouth stated in its Motion to Implement that it would not object, under specified circumstances, to the entry of an order that grants BellSouth's application but makes BellSouth subject to price regulation on a going forward basis does not constitute an amendment to the price regulation application. The Authority exercises its discretion and finds that October 1, 1995, is the appropriate effective date. Approving BellSouth's application for a price regulation plan with an effective date of October 1, 1995, is necessary to place BellSouth in the position that it would have been in had the Commission not erred, which is consistent with the Court of Appeals' opinion.⁶ October 1, 1995, is the effective date that BellSouth had requested in its application filed on June 20, 1995, and would have been the effective date of BellSouth's plan had the Commission acted in a manner consistent with the requirements of Tenn. Code Ann. § 65-5-209.

⁶ It also is consistent with the general purpose of a remand announced by the Court of Appeals in *Hoover v. Metropolitan Board of Zoning*, where the Court stated that the general purpose of remand is to "place the parties and the Agency in the position they would have been in had the agency not acted improperly.

As noted in *Getty v. Federal Savings & Loan Insurance Corporation*, the remand should not be used to place the petitioner in a better position. The Authority's decision here does not do that. Here, but for the errors of the Public Service Commission, BellSouth would have been operating pursuant to a price regulation plan sometime in 1995 with the initial rates being those existing as of June 6, 1995. This is supported by the Court of Appeals in its October 1, 1997 decision, when it stated that the Public Service Commission "should have found that BellSouth's existing rates were affordable under Tenn. Code Ann. § 65-5-209(a) and should have approved BellSouth's application for a price regulation plan based on BellSouth's rates existing on June 6, 1995 as required by Tenn. Code Ann. § 65-5-209(c)." 972 S.W.2d at 680.

The potential benefits of price regulation are numerous. Price regulation provides BellSouth with greater flexibility in pricing, allowing it to respond to competitive pressures and the changing cost structures of the telecommunications industry. Price regulation also provides sustained incentives for BellSouth to improve its economic performance through productivity increases and cost reductions. Price regulation encourages BellSouth to make appropriate investments and capacity expansion. These improvements should facilitate BellSouth's deployment of new service offerings desired by Tennessee consumers, while also providing BellSouth the opportunity to earn a return that is sufficient to attract necessary capital investment.⁷

Based on the foregoing and consistent with the mandate and the opinion of the Court of Appeals on remand of *BellSouth Telecommunications, Inc. v. Greer*, the Directors voted unanimously to approve BellSouth's application for a price regulation plan with an effective date of October 1, 1995, with the initial rates being those existing as of June 6, 1995. The Directors also

⁷ The comments contained in this paragraph were made by Director Greer.

voted unanimously to accept and adopt the terms offered in the Memorandum in Support of BellSouth Telecommunications, Inc.'s Motion to Implement Appellate Court's Mandate with the exception that all references to August dates be changed to December.

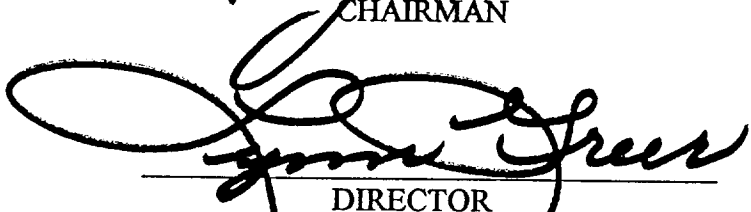
The motion to approve having been adopted unanimously by the Directors renders moot the Consumer Advocate's Motion to Begin Afresh.

IT IS THEREFORE ORDERED THAT:

1. BellSouth's application for a price regulation plan with an effective date of October 1, 1995 with the rates existing on June 6, 1995, is hereby approved.
2. BellSouth's price regulation plan shall be subject to the price regulation methodology stipulated to in *In re: United Telephone Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment*, Docket No. 96-01423.
3. Increases in BellSouth's initial rates for Basic Local Exchange Telephone Service shall not occur until December 1, 2002, consistent with Tenn. Code Ann. § 65-5-209(f).
4. Increases in BellSouth's rates for Call Waiting shall not occur until December 1, 2002, consistent with Tenn. Code Ann. § 65-5-209(h).
5. Annual adjustments in BellSouth's basic and nonbasic rates pursuant to Tenn. Code Ann. § 65-5-209(e) shall be calculated from December 1, 1998, and the calculation of the Service Price Index for basic and nonbasic services shall be based upon service volumes for the month of December for the year of the annual filing and upon service prices in effect on December 1, 1998 or as reset by the Authority under Tenn. Code Ann. § 65-5-207.
6. Annual adjustments in BellSouth rates for Interconnection Services pursuant to Tenn. Code Ann. § 65-5-209(g) shall be calculated from December 1, 1998.

7. The Motion to Begin Afresh filed by the Consumer Advocate is moot.
8. Any party aggrieved by the Authority's decision in this matter may file a Petition for Reconsideration with the Authority within ten (10) days from the date of this Order.
9. Any party aggrieved with the Authority decision in this matter has the right of judicial review by filing a Petition for Review in the Tennessee Court of Appeals, Middle Division, within sixty (60) days from and after the date of this Order.


CHAIRMAN


DIRECTOR


DIRECTOR

ATTEST:


EXECUTIVE SECRETARY

APPENDIX C

INCUMBENT LOCAL EXCHANGE COMPANIES 1998 STATISTICAL DATA

	CUSTOMERS			ACCESS LINES			REVENUES					
	Local		Business	Residential	Business	Total	Local			Long Distance		
	Residential	Business					Residential	Business	Total	Residential	Business	Total
BellSouth	1,789,492	204,115		1,911,066	758,964	2,670,030	477,708,000	547,067,000	1,024,775,000	238,164,000	333,539,000	571,703,000
UTSE	176,219	26,658		177,445	74,444	251,889	39,053,517	35,575,263	74,628,780	8,890,355	8,398,253	17,288,608
Citizens	69,876	10,072		72,925	23,416	96,341	13,754,245	11,095,903	24,850,148			17,959,558
TDS	67,931	8,909		71,480	21,200	92,680	19,718,899	16,465,398	36,184,297	18,656,689	3,400,218	22,056,907
TEC	N/A	N/A		11,304	2,338	13,642			835,280			8,103,225
Century	18,441	2,991		20,378	5,010	25,388	4,644,195	2,479,249	7,123,444	4,245,085	1,030,540	5,275,625
Ardmore	2,176	362		2,291	470	2,761	374,958	76,799	451,757	765,215	156,731	921,946
Loretto	4,873	682		4,843	731	5,574	775,312	235,076	1,010,388	N/A	N/A	N/A
United	10,856	1,328		10,856	1,482	12,338	2,140,857	264,600	2,405,457	4,671,870	577,422	5,249,292
Millington	N/A	N/A		19,871	4,132	24,003	6,247,079	1,695,546	7,942,625	4,202,095	1,140,683	5,342,778
Total	2,139,864	255,117		2,302,459	892,187	3,194,646	584,417,062	614,954,834	1,180,207,176	279,595,308	348,242,847	653,900,939

Note: Detailed statistical data for telephone cooperatives is not available since they are not regulated by the TRA.

^{A/} Citizens of Tennessee and Citizens of the Volunteer State
^{B/} Concord, Tellico, Tennessee Telephone and Humphreys County
^{C/} Crockett, Peoples and West Tennessee Telephone
^{D/} Adamsville, Clatborne and Collewah-Collegedale

TENNESSEE INCUMBENT LOCAL EXCHANGE COMPANIES

	Company	1998 Access Lines
1.	Ardmore Telephone	2,761
2.	BellSouth Telecommunications	2,670,030
3.	Ben Lomand Telephone Cooperative*	31,200
4.	Bledsoe Telephone Cooperative*	9,681
5.	CenturyTel Companies	25,388
6.	Citizens Telecommunication Companies	96,341
7.	DTC Communications*	18,274
8.	Highland Telephone Cooperative*	16,026
9.	Loretto Telephone	5,574
10.	Millington Telephone	24,003
11.	North Central Telephone Cooperative*	13,593
12.	Skyline Telephone Membership Corporation*	460
13.	TDS Telecom Companies	92,680
14.	Telephone Electronics Corporation Companies	13,642
15.	Twin Lakes Telephone Cooperative*	33,964
16.	United Telephone	12,338
17.	Sprint/United	251,889
18.	West Kentucky Telephone Cooperative*	2,143
19.	Yorkville Telephone Cooperative*	1,921

* Telephone cooperatives not subject to regulation of the TRA

SERVICE AREAS OF INCUMBENT LOCAL EXCHANGE CARRIERS

BellSouth Telecommunications

Adams-Cedar Hill	Dayton	Humboldt	Morristown	So. Cunningham
Arlington	Decatur	Huntington	Moscow	So. Fredonia
Ashland City	Dickson	Huntland	Mount Pleasant	So. Fulton
Athens	Dover	Jackson	Murfreesboro	So. Guthrie
Bean Station	Dyer	Jasper	Nashville	So. Oak Grove
Bells	Dyersburg	Jefferson City	Newbern	So. Pittsburg
Bent Creek	Eagleville	Jellico	Newport	Spencer Mill
Benton	East Sango	Kenton	Normandy	Spring City
Bethel Springs	Elkton	Kingston	Norris	Springfield
Big Sandy	Etowah	Kingston Springs	North Spring Hill	Spring Hill
Blanche	Fairview	Knoxville	Oak Ridge	Summertown
Bolivar	Fayetteville	LaFollette	Old Hickory	Surgoinsville
Brownsville	Flintville	LaGrange	Oliver Springs	Sweetwater
Bulls Gap	Fork Ridge	Lake City	Palmyra	Tiptonville
Camden	Franklin	Lawrenceburg	Paris	Trenton
Carthage	Fredonia	Lebanon	Petersburg	Triune
Cedar Hill	Gallatin	Lenoir City	Pleasant View	Troy
Centerville	Gatlinburg	Lewisburg	Portland	Tullahoma
Charleston	Georgetown	Lexington	Pulaski	Union City
Charlotte	Gibson	Loudon	Ridgely	Vanleer
Chattanooga	Gleason	Lyles	Ripley	Wartrace
Chestnut Hill	Goodlettsville	Lynchburg	Rockwood	Watertown
Clarksville	Grand Junction	Lynnville	Rogersville	Waverly
Cleveland	Greenback	Madisonville	Sango	West Vanleer
Clinton	Greenbrier	Manchester	Sante Fe	West Sweetwater
Collierville	Greenfield	Maryville	Savannah	White Bluff
Columbia	Halls	Mascot-Strawberry Plains	Selmer	White House
Copper Basin	Hampshire	Maynardville	Sevierville	White Pine
Covington	Harriman	McEwen	Sewanee	Whiteville
Cross Plains	Hartsville	McKenzie	Shelbyville	Whitwell
Culleoka	Henderson	Medina	Smyrna	Williamsport
Cumberland City	Hendersonville	Memphis	Sneedville	Winchester
Cumberland Gap	Henning	Michie	Soddy-Daisy	
Cunningham	Hohenwald	Middleton	Solway	
Dandridge	Hornbeak	Milan	Somerville	

SERVICE AREAS OF INCUMBENT LOCAL EXCHANGE CARRIERS

Adamsville (CenturyTel)	Concord (TDS)	Sprint United	Tennessee Telephone (Cont)
Adamsville	Concord	Baileton	Collinwood
Enville		Blountville	Comersville
Milledgeville	Crockett (TEC)	Bluff City	Darden
Shiloh	Alamo	Bristol	Decaturville
Ardmore Telephone Company	Friendship	Butler	Halls Cross Roads
Ardmore	Maury City	Church Hill	Lavergne
McBurg		Elizabethton	Linden
Minor Hill	Humphreys County (TDS)	Erwin	Lobelville
	New Johnsonville	Fall Branch	Mt. Juliet
Citizens Telecom of Tennessee		Greeneville	Parsons
Cookeville	Loretto Telephone Company	Hampton	Sardis
Crossville	Ethridge	Johnson City	Scotts Hill
Dresden	Leoma	Jonesborough	Waynesboro
Latham	Loretto	Kingsport	
Martin	St. Joseph	Limestone	United Telephone Company
McMinnville	Five Points	Midway (Sullivan County)	Belfast
Monterey		Midway (Washington County)	Chapel Hill
Palmer'sville	Millington Telephone Company	Mosheim	College Grove
Pleasant Hill	Drummonds	Mountain City	Estill Springs
Sharon	Mason	Roan Mountain	Flat Creek
Sidonia	Millington	Stoney Creek	Fosterville
Sparta	Munford	Sullivan Gardens	Nolensville
Tansi	Rosemark		Unionville
	Shelby Forest	Tellico (TDS)	
Citizens Telecom of Volunteer State	Stanton	Ball Play	West Tennessee Telephone (TDS)
Claxton		Coker Creek	Atwood
Powell	Ooltewah-Collegedale (CenturyTel)	Englewood	Bradford
Rutledge	Apison	Niota	Rutherford
Tate Springs	Collegedale	Riceville	Trezevant
Washburn	Ooltewah	Tellico Plains	
		Vonore	
Claiborne (CenturyTel)	Peoples (TEC)		
New Tazewell	Erin	Tennessee Telephone (TDS)	
Sharps Chapel	Henry	Bruceston	
	Tennessee Ridge	Clifton	

SERVICE AREAS OF TELEPHONE COOPERATIVES
(Not Regulated by the TRA)

Ben Lomand Telephone Cooperative Beech Grove Beersheba-Altamount Bon Decroft Centertown Dibrell Doyle Hillsboro Laager McMinnville Rural Monteagle Old Zion Pelham Rock Island Sparta Rural Spencer Tracy City Viola Bledsoe Telephone Cooperative College Station Dunlap Fall Creek Falls Nine Mile Pikeville DCT Communications Alexandria Auburntown Gordonsville Liberty Milton Norene Smithville Temperance +Hall Woodbury	DCT Communications (Cont) Woodland Highland Telephone Cooperative Deer Lodge Huntsville Oakdale Oneida Petros Robbins Sunbright Wartburg North Central Telephone Cooperative Bethpage Defeated Green Grove Hillsdale Lafayette Oak Grove Pleasant Sahde Red Boiling Springs Westmoreland Scottsville Rural (KY) Skyline Telephone Membership Cooperation Shady Valley Twin Lakes Telephone Cooperative Baxter Byrdstown Celina Chestnut Mound Clarkrange Cookeville South Crawford	Twin Lakes Telephone Cooperative (Cont) Gainesboro Granville Highland Jamestown Livingston Moss North Springs Rickman West Kentucky Telephone Cooperative Cottage Grove Cypress Purveyar Yorkville Telephone Cooperative Brazil Mason Hall Trimble Yorkville
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TENNESSEE LOCAL RESELLERS

Company Name		Company Location
1. 1-800 RECONEX, Inc.		Hubbard, OR
2. American Network Exchange, Inc.		Orlando, FL
3. American Telecommunication		Nashville, TN
4. Ameritech Communications International,		Rosemont, IL
5. Annex, Inc.		Pleasant View, TN
6. Atlas Communications, Ltd.		Blue Bell, PA
7. Business Telecom, Inc.		Raleigh, NC
8. Cash to Go, LLC		Murfreesboro, TN
9. Cellular Concepts & Paging, Inc.		Memphis, TN
10. Comm South Companies, Inc.		Arlington, TX
11. Discount Communications		Memphis, TN
12. East Tennessee Phone Service		Lenoir City, TN
13. Easton Telecom Services, Inc.		Richfield, OH
14. Excel Communications, Inc.		Dallas, TX
15. Express Connection Telephone Services		Nashville, TN
16. EZ Phone, Inc.		Akron, OH
17. EZ Talk Communications, Inc.		Stafford, TX
18. Fast Connections, Inc.		Dallas, TX
19. Frontier Telemanagement		Rochester, NY
20. GE Capital Communications Services		Atlanta, GA
21. Group Long Distance, Inc.		Ft. Lauderdale, FL
22. Image Access, Inc.		Metairie, LA
23. Intellical Operator Services, Inc. (IOS)		Dallas, TX
24. Jerry LaQuiere		Antioch, TN
25. John C. Chapman		Bartlett, TN
26. Lawrence Hansbro d/b/a Push Button		Augusta, GA
27. LDM Systems, Inc.		Kalamazoo, MI
28. Long Distance Direct Holdings, Inc.		Pearl River, NY
29. Max-Tel Communications, Inc.		Alvord, TX
30. NET-tel Corporation		Reston, VA
31. North American Telecommunication		Roslyn Heights,
32. North American Telephone Network, Inc.		Atlanta, GA
33. NOW Communications, Inc.		Jackson, MS
34. NuStar Communications Corp.		Nashville, TN
35. Omniplex Communications Group, LLC		Chesterfield, MO
36. OnePoint Communications, Georgia, LLC		Bannockburn, IL
37. Opus Correctional, Inc.		Framingham, MA
38. P.V. Tel., LLC		Kingsport, TN
39. Paramount International		Vista, CA
40. Phone-Link, Inc.		LaGrange, KY

Company Name		Company Location
41. Preferred Carrier Services, Inc.		Dallas, TX
42. Quick-Tel Communications, Inc.		Boyd, TX
43. Scirocco Communications, LLC		Knoxville, TN
44. Shared Communications Services, Inc.		Salem, OR
45. SouthNet Telecomm Services, Inc.		Marietta, GA
46. State Communications, Inc.		Greenville, SC
47. TEL-LINK, LLC		Bradenton, FL
48. Tel-Save, Inc. d/b/a The Company		New Hope, PA
49. Telco Holdings d/b/a Dial & Save		Chantilly, VA
50. TeleSource		Dickson, TN
51. Tele-SYS, Inc. d/b/a Access America		Oak Ridge, TN
52. TeleConex, Inc.		Pensacola, FL
53. Telephone Company of Central Florida,		Lake Mary, FL
54. Tennessee Phone Service		Nashville, TN
55. The Video Center, Inc.		Murfreesboro,
56. Time Warner Communications of the Mid-		Nashville, TN
57. Touch 1 Communications, Inc.		Atmore, AL
58. U.S. Dial Tone, Inc.		San Antonio,
59. U.S. Telco, Inc.		Dallas, TX
60. UniDial Incorporated		Louisville, KY
61. United Communications Systems, Inc.		Chicago, IL
62. Vast-Tel Communications, Inc.		Bridgeport, TX
63. Z-Tel Communications, Inc.		Tampa, FL

TENNESSEE LONG DISTANCE RESELLERS

Company Name		Company Name	
1.	1-800 RECONEX, Inc.	41.	Central Payphone Services, Inc.
2.	360 Communications Company	42.	Century Telecommunications, Inc.
3.	ACC National Long Distance Corp.	43.	CFW Telecommunications Services, Inc.
4.	Access Network Services, Inc.	44.	Charities Network International, Inc.
5.	Access Point, Inc.	45.	Cherry Communications, Inc. ("CCI")
6.	Advanced Telecommunications Network,	46.	CIMCO Communications, Inc.
7.	Affinity Corporation	47.	Cincinnati Bell Long Distance, Inc.
8.	Alternative Long Distance, Inc. d/b/a	48.	Citizens Telecomm. Co., dba Citizens
9.	American Farm Bureau, Inc. d/b/a The	49.	Cleartel Communications
10.	American International Telephone, Inc.	50.	C-Net Communications
11.	American Long Lines, Inc.	51.	Coast International, Inc.
12.	American Network Exchange, Inc.	52.	Coastal Telecom Limited Liability
13.	American Tel Group, Inc.	53.	Colorado River Communications Corp.
14.	American Telco, Inc.	54.	Comdata Telecommunications Services,
15.	American Telecommunications	55.	Common Concerns, Inc.
16.	American Telecommunications Systems,	56.	Communications TeleSystems
17.	Americom Technologies, Inc.	57.	CommuniGroup of Jackson, Inc.
18.	Amer-I-Net Services, Corp.	58.	Computer Telephone Corp.
19.	Ameritech Communications	59.	Connect America Communications, Inc.
20.	AmeriVision Communications, Inc.	60.	ConQuest Operator Services Corp.
21.	Apollo Communications Services, LLC	61.	Consolidated Communications, Inc.
22.	Association Administrators, Inc.	62.	Corporate Services Telecom, Inc.
23.	ATCALL, Inc.	63.	CTC Long Distance Services, Inc.
24.	Athena International, L.L.C.	64.	CTN Telephone Network, Inc.
25.	Atlas Communications, Ltd.	65.	D.D.D. Calling, Inc.
26.	ATN Communications Incorporated	66.	DeltaCom, Inc.
27.	Bell Atlantic Communications, Inc.	67.	DeltaTel, inc.
28.	BellSouth Public Communications, Inc.	68.	Discount Network Services, Inc.
29.	Ben Lomand Communications, Inc.	69.	Discounted Long Distance, Inc.
30.	BLT Technologies, Inc.	70.	Eastern Telecommunications, Inc.
31.	Brittan Communications International	71.	Easton Telecom Services, Inc.
32.	Budget Call Long Distance, Inc.	72.	Eclipse Telecommunications, Inc.
33.	Buehner-Fry, Inc. dba Resort Operator	73.	EconoPhone, Inc.
34.	Business Discount Plan, Inc.	74.	EqualNet Corporation
35.	Business Options, Inc.	75.	Excel Communications, Inc.
36.	Business Telecom, Inc.	76.	Federal TransTel, Inc.
37.	Cable & Wireless, Inc.	77.	First National Services Corp. (FNSC)
38.	Call Plus, Inc.	78.	Five Star Telecom, Inc.
39.	Calls for Less, Inc. d.b.a. CFL, Inc.	79.	Florida Network, U.S.A., Inc.
40.	Capital Long Distance	80.	Frontier Communications International

TENNESSEE LONG DISTANCE RESELLERS

Company Name		Company Name	
81.	Frontier Communications Services	121.	National Telephone & Communications,
82.	GE Capital Communication Services	122.	NeTel, Inc.
83.	Global Tel Link	123.	NET-tel Corporation
84.	Group Long Distance, Inc.	124.	Network Enhanced Technologies, Inc.
85.	GTE Communications Corp.	125.	Network Operator Services, Inc.
86.	Gulf Long Distance, Inc.	126.	Network Plus, Inc.
87.	Hertz Technologies, Inc.	127.	Norlight, Inc.
88.	Highland Communications Corpotation	128.	Norstan Network Services, Inc.
89.	Hi-Plains NTS Communication, Inc.	129.	NOSVA, Limited Partnership
90.	Home Owners Long Distance, Inc.	130.	OLS, Inc.
91.	IdealDial Corp.	131.	One Star Long Distance, Inc.
92.	IDT Corporation	132.	One Step Billing, Inc.
93.	Inacom Communications, Inc.	133.	Operator Service Co.
94.	Independent Network Services	134.	Optex, Inc.
95.	Innovative Telecom Corporation	135.	OPTICOM
96.	Intelicom International Corp	136.	Opus Correctional, Inc.
97.	Intelicall Operator Services, Inc. (IOS)	137.	Pantel Communications, Inc.
98.	Intelnet International Corp.	138.	Pay Tel Communications, Inc.
99.	International Telecom, Ltd.	139.	Phoenix Network, Inc.
100.	International Telecommunications Corp.	140.	Preferred Carrier Services, Inc.
101.	Inter-Tel NetSolutions, Inc.	141.	Premiere Communications, Inc.
102.	IXC Long Distance	142.	Primus Telecommunications, Inc.
103.	J D Services, Inc.	143.	Professional Communication Management
104.	Key Communications Management, Inc.,	144.	QCC, Inc.
105.	L.D. Services, Inc.	145.	Quest Telecommunications, Inc.
106.	LCI International Telecom, Corp.	146.	Qwest Communications Corporation
107.	LDC Telecommunications, Inc.	147.	RCN Long Distance Company
108.	LDM Systems, Inc.	148.	RRV Enterprises, Inc. d/b/a Consumer
109.	Least Cost Routing, Inc.	149.	RSL COM U.S.A., Inc.
110.	Long Distance Billing	150.	SBR, Inc.
111.	Long Distance International, Inc.	151.	Shared Communications Services, Inc.
112.	Long Distance of Michigan, Inc.	152.	SmarTalk TeleServices, Inc.
113.	Matrix Telecom, Inc.	153.	SNET America, Inc.
114.	Maxima Communications Corp.	154.	Southeast Telephone, L.P
115.	McLeodUSA	155.	Southeastern Network Services, LLC
116.	Minimum Rate Pricing, Inc.	156.	SouthernNet, Inc./Teleconnect
117.	Mobilemedia of Tennessee	157.	Southwestern Bell Communications
118.	MTC Telmanagement Corp.	158.	Speer Virtual Media, Ltd.
119.	National Accounts, Inc.	159.	Starlink Communications, LLC
120.	National Communications Association,	160.	Switched Services Communications, L.L.C.

TENNESSEE LONG DISTANCE RESELLERS

Company Name	
161. Telaleasing Enterprises, Inc.	200. Value Tel, Inc.
162. Telco Holdings dba Dial & Save	201. VarTec Telecom, Inc.
163. Telco Partners, Inc.	202. VIP Telephone Network, Inc.
164. Telec, Inc.	203. Vista Group International, Inc.
165. Telecare	204. Westinghouse Communications
166. Telecom One, Inc.	205. Winstar Gateway Network, Inc.
167. Telecommunications Company of the	206. Working Assets Funding Service, Inc.
168. Telegroup, Inc.	207. World Wide Communications, Inc.
169. Telescan, Inc.	208. Wright Business, Inc.
170. Tele-Sys, Inc. d/b/a Access America	209. Xtracom, Inc.
171. Tel-Save, Inc. d/b/a The Phone Company	210. Zenex Long Distance, Inc.
172. Telescope USA, Inc.	
173. Teltrust Communications	
174. Tennessee Phone Service	
175. The Furst Group, Inc.	
176. Thrifty Call, Inc.	
177. TLX Communications, Inc. (Telamerica)	
178. TMO Communications Co.	
179. Total Tel, Inc.	
180. Touch 1 Communications, Inc.	
181. Touch 1 Long Distance, Inc.	
182. Transcommunications, Inc.	
183. TresCom U.S.A., Inc.	
184. TTI National, Inc.	
185. U S WEST Interprise America, Inc.	
186. U S West Long Distance, Inc.	
187. U.S. Osiris Corporation	
188. U.S. Republic Communications, Inc.	
189. UniDial Incorporated	
190. United Telephone Long Distance, Inc.	
191. US South Communications, Inc.	
192. US WATS, Inc.	
193. USA Global Link, Inc.	
194. USA Tele Corp.	
195. USLD Communications, Inc.	
196. USN Communications Long Distance, Inc.	
197. UStel, Inc.	
198. USX Consultants, Inc.	
199. UTC Long Distance, L.L.C.	

As of 12/31/97

Source: Form UD-16 (Companies reporting Tennessee intrastate revenue)

APPENDIX G

TENNESSEE CELLULAR PROVIDERS

	Company
1.	360° Communications Company of TN No. 2
2.	Advantage Cellular Systems, Inc.
3.	BellSouth Mobility, Inc.
4.	Chattanooga Cellular Telephone Company
5.	Chattanooga MSA Limited Partnership
6.	GTE Mobilnet of Clarksville, Inc.
7.	GTE Mobilnet of Nashville, Inc.
8.	GTE Mobilnet of Tennessee, Inc.
9.	H.S. Communications, Inc.
10.	Knoxville Cellular Telephone Company
11.	M-T Cellular, Inc.
12.	Memphis Cellular Telephone Company
13.	Memphis SMSA Limited Partnership
14.	Tennessee RSA # 8 Limited Partnership
15.	Tennessee RSA Limited Partnership
16.	Tennessee RSA #3 Limited Partnership
17.	Tennessee RSA #4 Sub 2, Inc.
18.	U.S. Cellular Telephone Company (Greater Knoxville)
19.	Westel-Milwaukee Company, Inc.
20.	Yorkville Telephone Cooperative, Inc.

TENNESSEE PCS PROVIDERS

	Company
1.	BellSouth Personal Communications, Inc.
2.	Powertel Memphis Licenses, Inc.
3.	Sprint Spectrum, L.P.

SERVICE AREAS OF TENNESSEE CABLE TELEVISION PROVIDERS

Aerial Cablevision, Inc. New Johnsonville	Comcast (Cont)	Falcon	Helicon (Cont)
Annox Pleasant View	Gatlinburg Greenbrier Guys Harriman Jacksboro Kingston Knoxville Kodak LaFollette Lake City Lakesite Lookout Mountain Michay Norris Parrottville Pigeon Forge Pittman Center Red Bank Riceville Ridgeside Rockford Rockwood Sevierville Signal Mountain Soddy Daisy Townsend Walden Walden Creek Wears Valley	Brighton Brownsville Burlieson Covington Dyer Garland Gates Gilt Edge Halls Henning Kenton Ripley Rutherford So. Fulton Fannon Arthur Cumberland Gap Harrogate Lone Mountain New Tazewell Shawnee Speedwell Tazewell Frontiervision Friendsville Greenback Greeneville Loudon	Crandall Dalton Dayton Decatur Eton Georgetown Guild Hale Town Harrison Jasper Kimball Kingston LaFayette Lyerly Menlo New Hope Powells Crossroads Sequatchie Sykline So. Pittsburg Somerville Stevenson Ten Mile Trenton Trion Whiteside Whitwell Wildwood
Benton County Cablevision Big Sandy Camden Eva	Communicomm Services Jamestown Wartburg	Gainesboro CATV, Inc. Gainesboro	HI-Country Cable Roane Mountain
Bledsoe Telephone Co-Op Dunlap Pikeville	Dresden Cable, Inc. Dresden	Helicon Cable Communications Bridgeport Calhoun Charleston Chatsworth Cloud Land	Marcus Cable Baneberry Bean Station Blountville Bristol Dandridge Elizabethton Jefferson City
Cablevision Huntland Mountain City	Falcon Cable Bolivar Bradford		
Celina Cable Communications Celina Red Boiling Springs Pikeville			
Charter Ashland City Clarksville			
Comcast Communications Athens Benton Bybee Chattanooga Cobbly Nob Collegedale Condo Villas Copper Hill Cosby Ducktown East Ridge Etowah			

SERVICE AREAS OF TENNESSEE CABLE TELEVISION PROVIDERS

Marcus (Cont)	Intermedia (Cont)	Intermedia (Cont)	Millington CATV (Cont)	Rifkin & Associates (Cont)
Johnson City Morristown New Market Newport Sneedville White Pine	Greenfield Henderson Hendersonville Hohenwald Hollow Rock Huntingdon Iron City Joelton Kingsport Kingston Springs LaFayette Lakewood Lavergne Lenoir City Leoma Lewisburg Lexington Loretto Loudon Lynchburg Lynn Garden McEwen McKenzie Madisonville Martin Maryville Milan Monterey Mount Carmel Mount Juliet Mount Pleasant Murfreesboro Nashville Newsome Station Nolensville Oak Hill Parsons Pegram Pigeon Forge Red Boiling Springs	Ridgetop Rives Rogersville St. Joseph Savannah Sevierville Sharon Smithville Smyrna Springfield Sullivan Gardens Sweetwater Trezvant Union City Waverly Waynesboro West Point White Bluff Winchester Woodbury Woodland Mills Mid-South Cable TV, Inc. Birchwood College Grove Crab Orchard Crossville Eagleville Monterey Nolensville Ooltewah Pleasant Hill Triune Millington CATV, Inc. Atoka Memphis Millington Murford	Pat's Cable Company Linden Lobelville Scotts Hill Phoenix Cable, Inc. Fairfield Glade Post Newsweek Cable Co Dyersburg Finley Fowlkes Tigrett Rifkin & Associates Alexandria Algood Baxter Bluff City Centertown Coalmont Columbia Cookeville Culleoka Dowelltown Doyle Fayetteville Gordonsville Gruettli-Laager Hampshire Hickory Hill Kingsport Lawrenceburg Lebanon Liberty McMinville Manchester Monteague Morrison Mount Pleasant	Palmer Paris Piney Flats Pulaski Santa Fe Sewanee Shelbyville Sparta Spencer Spring Hill Springville Summertown Thompson Station Tracy City Tullahoma Viola Watauga Watertown Williamsport Scripps Howard, Inc. Afton Bulls Gap Chuckey Erwin Gray Greeneville Hampton Harmony Johnson City Jonesboro Livingston Morristown Mosheim Rheatown Russellville Tusculum Valley Forge

SERVICE AREAS OF TENNESSEE CABLE TELEVISION PROVIDERS

SRW Cablevision Butler Erwin Hampton Laurel Bloomery Trade Spring City Cable TV, Inc. Spring City Tele-Media of Green River Cross Plains Millersville White House Tennessee Cablevision, Inc. Claxton Clinton Oak Ridge Oliver Springs South Clinton Tennessee Valley Cable Smithville	Time Warner (Cont) Lakeland Malesus Mason McNairy Memphis Middleton Moscow Muay City Newbern Oakland Piperton Rossville Saulsbury Selmer Somerville Stanton Trimble Troy Whiteville Williston Trenton TV Cable Company Trenton Triax Cablevision USA Horn Beak Ridgely Samburg Tiptonville Wynnborg United Artists Warmath Communications, Inc. Humboldt Medina			
Time Warner Communications Adamsville Alamo Arlington Bartlett Bells Bemis Bethel Springs Braden Camden Collierville Galloway Germantown Grand Junction Jackson LaGrange				

Source: Tennessee Cable Telecommunications Association

TENNESSEE LOCAL AND REGIONAL INTERNET ACCESS PROVIDERS

Access America Telephone Co. accessU.S., Inc. AceLink Communications, LLC Advantage Web Aeneas Internet Services, LLC Ardmore Telephone Co., Inc. Awesome Net at Tennessee Tech University BellSouth.net, Inc. Ben Lomand Rural Telephone Cooperative, Inc. Bledsoe Telephone Cooperative, Inc. BlitzNet Online Communications, Inc. BMR Communications, Inc. Campbell County On-Line / Preferred Sys., Inc. Capital City Cyberlink Century Telephone Chattanooga Data Connection, Inc. Clarksville InterNET Services Compu-Net Enterprises Computer Cafe Internet Services Computerized Control Concepts ComStar USA, Inc. Connect 200 Cybercast Internet Services Cybersoft Systems (D) Datatek International, Inc. Dataworld / Net-Express Digex, Inc. (D) DTC Communications EdgeNet Media, LLC Electronic Communication Systems Electrotex, Inc. Esper Internet Services Final Frontier, The First Internet Communications, LLC First Internet Resources, Inc. Gekko Internet Services, Inc. GoldSword Systems Greene County Online Heart of Tennessee Computer Communications Network Henderson County On-Line, Inc. Higher Technology Services, Inc. / Chattanooga Online	Highland Telephone Cooperative Hopkinsville Internet Service ICX online Iglou Internet Services Info Avenue Internet Services, LLC InterMedia Internet Services Internet Communications Group Internet Services Corp. Internet Services of West Tennessee Interstate 2000, Inc. ISDN-Net, Inc. KidSurf Online Knightwave Technologies KnoxNet, Inc. Knoxville News-Sentinel Co., The Knoxville-Oak Ridge Regional Network, The (KORRnet) Lamar Network Service Lock-Net Internet Services / Infinity Computer Systems LogOn Computer Services Loretto Telephone Co., Inc. LunaWeb, Inc. Magibox, Inc. Martek Computer Co. Maryvale College Memphis Online Mid-South Connections Mid-South Online Middle Tennessee Internet Service Middle Tennessee Internet Service at Belmont Univ. Midwest Internet Motion, LLC MTSU University MultiPro Network, The N2 The Net Nashville Exchange, The Net Services Net-Serv / CMS, Inc. NetAccess, Inc. NetAware NetEase Internet Access Service / Mesa Partners NetLinX Technologies	NetStar Communications Group NewsChannel 5 Online (Internet Services) Newsite Internet Services North Central Telephone Cooperative, Inc. OC96, Inc. (D) Pixelation Data Services, Inc. Planet Connect Internet Point of View Internet Services & Solutions Preferred Internet, Inc. Q Systems, Inc. (D) Rnet Internet Services SkyQuest SoftTek, Inc. StarNet, Inc. Support Engineering Synapse, LLC T-Net TDSnet Internet Services Telalink Corp. TeleSouth Network Tennessee Networking Systems Tennessee Professional Web Services Tennessee State University Theta Systems, Inc. Third Wave Technologies TN Web, LLC Traders' Connection, Inc. Twin Lakes Telephone Cooperative Corp. United States Internet, Inc. United States POP Network United Telephone Co. UTC On Line at UT-Chattanooga Valley Internet, Inc. ValleyNet (D) Virtual Enterprises, Inc. Virtual Interactive Center Vnet Internet Access, Inc./CT Comm. Volunteer Network Services, Inc. Volunteer State Internet Voyager Online, LLC Web Net Memphis	WebbSource WingNET Internet Services WorldNet Communications World Spice Technologies
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Source: www.thedirectory.org

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

April 9, 1998

IN RE:

AVR OF TENNESSEE, L.P. d/b/a HYPERION OF
 TENNESSEE, L.P., APPLICATION FOR A
 CERTIFICATE OF PUBLIC CONVENIENCE AND
 NECESSITY TO EXTEND TERRITORIAL AREA
 OF OPERATIONS TO INCLUDE THE AREAS
 CURRENTLY SERVED BY TENNESSEE
 TELEPHONE COMPANY

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) Docket No.: 98-0001
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**ORDER DENYING HYPERION'S APPLICATION FOR A CERTIFICATE OF PUBLIC
 CONVENIENCE AND NECESSITY TO EXTEND ITS SERVICE TERRITORY INTO
 AREAS CURRENTLY SERVED BY TENNESSEE TELEPHONE COMPANY**

On March 10, 1998, this matter came before the Tennessee Regulatory Authority (the "Authority") at a regularly scheduled and properly noticed Directors' Conference, for a decision on the Application of AVR of Tennessee, L.P. d/b/a Hyperion of Tennessee, L.P. ("Hyperion") for a Certificate of Public Convenience and Necessity ("CCN") to extend its territorial area of operations to include the areas currently served by Tennessee Telephone Company. Hyperion's pleading will be referred to hereinafter as the "Application."

BACKGROUND

On January 2, 1998, Hyperion filed its Application, pursuant to Tenn. Code Ann. § 65-4-201(b), and requested that the Authority interpret Section 253(a) of the federal Telecommunications Act of 1996 (the "Act") as a prohibition against the enforcement of Tenn. Code Ann. § 65-4-201(d), to the extent that Tenn. Code Ann. § 65-4-201(d) would deny

Hyperion the ability to provide competing telecommunications services within the service territory of Tennessee Telephone Company.¹ On January 14, 1998, Tennessee Telephone Company, Concord Telephone Company, Tellico Telephone Company and Humphreys County Telephone Company (collectively "the Intervenors") jointly petitioned to intervene in this matter.

On February 3, 1998, this matter came to be heard at a properly noticed Directors' Conference for the purposes of considering the joint intervention petition of the Intervenors and appointing a pre-hearing officer. The Directors unanimously granted the joint petition to intervene, and, at the suggestion of the parties, determined that this matter could be resolved without the necessity for the appointment of a pre-hearing officer. The parties were instructed to file initial and reply briefs on the legal issues involved in this matter, and the same were timely filed in accordance with the Authority's schedule.² The briefed positions of the parties may be summarized as follows:

HYPERION:

1. By order of the Authority's predecessor, the Tennessee Public Service Commission (the "TPSC"), Hyperion holds a CCN to provide telecommunications services as a competing telecommunications provider throughout Tennessee, except in those areas served by an incumbent local exchange telephone company with fewer than 100,000 total access lines in Tennessee.³ The TPSC's Order, relying upon Tenn. Code Ann. § 65-4-201(d), restricts Hyperion

¹ On the authority of Tenn. R. Civ. P. 24.04, the Authority's Executive Secretary provided notice to the Tennessee Attorney General that the validity of Tenn. Code Ann. 65-4-201(d) was drawn into question in this matter. The Attorney General did not elect to participate, either by written argument or through oral argument.

² By letter dated February 4, 1998, Hyperion waived any rights to enforce the statutory deadline provided in Tenn. Code Ann. § 65-4-201 requiring the entry of an order no more than sixty (60) days from the filing of the application for certification of a competing telecommunications service provider.

³ Public Service Commission Order entered in Docket No. 94-00661 on August 24, 1995, p.9, ¶15, attached to Hyperion's Application as Exhibit 1.

from competing against Tennessee Telephone Company in its protected service area.⁴ In so doing, the TPSC granted to Tennessee Telephone Company a protected monopoly status that undermines competition in contradiction of the goals of the Act.

2. In In re Silver Star Telephone Company, Inc. Petition for Preemption and Declaratory Ruling (“Silver Star”),⁵ the Federal Communications Commission (“FCC”) ruled that 47 U.S.C. § 253(a) “at the very least proscribes State and local legal requirements that prohibit all but one entity from providing telecommunications services in a particular State or locality.”⁶ Tenn. Code Ann. § 65-4-201(d) is a proscribed state legal requirement when it is applied to Hyperion for the purpose of prohibiting Hyperion’s access to Tennessee Telephone Company’s service area.

3. The FCC’s position in In re the Public Utility Commission et. al. Petition for Declaratory Ruling and/or Preemption of Certain Provisions of the Texas Public Utility Regulatory Act of 1995 (“the Texas Preemption Decision”)⁷ confirms the FCC’s stated intention to preempt state statutes such as Tenn. Code Ann. § 65-4-201(d), if and/or when such statutes are applied by state agencies to prohibit or have the effect of prohibiting local exchange carriers such as Hyperion from providing telecommunications services within the state.

4. The Supremacy Clause of Article VI of the Constitution of the United States provides Congress with the power to preempt state law. Among other times, preemption may

⁴ The TPSC’s Order did not restrict Hyperion from seeking the voluntary cooperation of Tennessee Telephone Company in opening its service area to cooperation, nor did it purport to limit Hyperion’s entry into that service area upon any other action of Tennessee Telephone Company as provided in Tenn. Code Ann. § 65-4-201(d).

⁵ Memorandum Opinion and Order, FCC 97-336, CCB Pol 97-1 (September 24, 1996) (attached to Hyperion’s Application as Exhibit 3).

⁶ *Id.* at ¶ 38.

⁷ Memorandum Opinion and Order, FCC 97-346, CCB Pol 96-13, 96-14, 96-16, and 96-19 (October 1, 1997). This is a combined case involving the petitions of numerous parties.

occur when Congress, in enacting a federal statute, expresses a clear intent to preempt state law, or when there is an actual or outright conflict between federal and state law. Preemption may result not only from action taken by Congress itself, but also from a federal agency acting within the scope of its congressionally delegated authority.

5. Tenn. Code Ann. § 65-4-201(d) has been preempted by Congress' enactment of 47 U.S.C. § 253(a) and by the FCC's action in Silver Star and the Texas Preemption Decision.

6. Under 47 U.S.C. §§ 251(a) and 251(b), "both Hyperion and Tennessee Telephone Company have the obligation to provide each other with interconnection, resale, number portability, dialing parity, and access to rights-of-way."⁸ Hyperion seeks to enforce its rights under those sections of the Act and to "offer its own services over its own facilities."⁹

7. 47 U.S.C. § 251(c) imposes additional obligations on incumbent local exchange carriers; however, Hyperion does not seek to enforce such additional obligations on Tennessee Telephone Company at this time. Specifically, Hyperion does not seek interconnection under 47 U.S.C. § 251(c)(2), unbundled access to network elements under 47 U.S.C. § 251(c)(3), resale of retail services at wholesale rates under 47 U.S.C. § 251(c)(4) or collocation under 47 U.S.C. § 251(c)(6).

8. 47 U.S.C. § 253(b) provides limited protection for certain state requirements; however, any such requirements must be competitively neutral and consistent with 47 U.S.C. § 254, and necessary to preserve and advance universal service, to protect public safety and welfare, to ensure continued quality of telecommunication services and to safeguard the rights of consumers. The FCC has determined that the requirements of Section 253(b) were not met in Silver Star and the Texas Preemption Decision, and the conclusion must be the same in this case

⁸ Hyperion's Application, p.9.

⁹ Id.

because the incumbent protection provisions already preempted by the FCC are virtually identical to Tenn. Code Ann. § 65-4-201(d).

9. By allowing Hyperion into Tennessee Telephone Company's service area, the goals of the Tennessee legislature will be furthered and the public will be generally benefited by increased competition, access to new technologies, increased efficiencies and cost savings.

THE INTERVENORS:

1. The Authority is a state regulatory agency charged with enforcing the laws of Tennessee, including Tenn. Code Ann. § 65-4-201(d). If the Authority applies Tenn. Code Ann. § 65-4-201(d) to the case at hand, Hyperion's application must be denied.

2. The Authority may not determine whether Tenn. Code Ann. § 65-4-201(d) has been preempted by federal law because an administrative agency does not have the power to declare a statute void or otherwise unenforceable. Moreover, administrative agencies have considerable factual and technical expertise within their fields, but they are not designed to engage in rigorous analysis of complex legal issues like preemption.

3. Hyperion's application constitutes a facial constitutional challenge to the Tennessee statute, and Richardson v. Tennessee Board of Dentistry, 913 S.W.2d 446, 454 (Tenn. 1995) held that "[t]he facial constitutionality of a statute may not be determined by an administrative tribunal in an administrative proceeding."

4. The Authority is not bound by the FCC's decision in Silver Star. In that proceeding, the FCC was presented only with the question of whether a Wyoming statute violates subsections (a) or (b) of 47 U.S.C. § 253. It did not consider whether Tenn. Code Ann. § 65-4-201(d) violates subsections (a) or (b) of 47 U.S.C. § 253. Moreover, as two (2) petitions for reconsideration are still pending in the Silver Star case, the FCC's decision is not a final ruling.

5. 47 U.S.C. § 253(d) envisions that preemption determinations should be made on a case by case basis by the FCC, after notice and an opportunity for public comment can be had. The FCC has not yet reviewed Tennessee's statute, and no notice and hearing have been had at the FCC level on the enforceability of Tennessee's statute.

6. The Act does not contain an express provision that mandates preemption of Tenn. Code Ann. § 65-4-201(d). The sections of the federal law cited by Hyperion and relied upon by the FCC in Silver Star do not require the preemption of state laws limiting competitive access to rural markets served by small incumbent local exchange telephone companies.

7. Hyperion claims it does not presently seek interconnection with Tennessee Telephone Company under 47 U.S.C. § 251(c); however, Hyperion has made inconsistent statements in this regard to Tennessee Telephone Company. Thus, the Authority should not permit Hyperion to seek interconnection pursuant to 47 U.S.C. § 251(c). If the Authority decides to grant Hyperion's application, and should later be faced with a request for interconnection pursuant to 47 U.S.C. § 251(c), then the Authority should refuse to terminate Tennessee Telephone Company's rural carrier exemption provided for by 47 U.S.C. § 251(f)(1).

ACTION BY THE AUTHORITY¹⁰

This matter came next to be heard on March 10, 1998, at a regularly scheduled Directors' Conference. Without oral argument of the parties, but after review of the record, the Authority unanimously agreed that Richardson v. Tennessee Board of Dentistry, 913 S.W.2d 446 (Tenn. 1995) did not preclude the Authority from deciding the issues in this matter, as the Authority considered Hyperion's Application to be an "as applied" challenge to the constitutionality of Tenn. Code Ann. § 65-4-201(d), rather than a challenge to the facial constitutionality of said statute.

On the preemption issue, the Authority voted 2-1 in favor of denying Hyperion's Application.¹¹ As a preface to acting on Hyperion's Application, Director Malone, expressing the majority view, stated:

¹⁰ The statutes at issue in this matter provide in part as follows:

Tenn. Code Ann. § 65-4-201(d):

"Subsection (c) is not applicable to areas served by an incumbent local exchange telephone company with fewer than 100,000 total access lines in this state unless such company voluntarily enters into an interconnection agreement with a competing telecommunications service provider or unless such incumbent local exchange telephone company applies for a certificate to provide telecommunications services in an area outside its service area existing on the June 6, 1995."

47 U.S.C. § 253:

"(a) IN GENERAL. - No State or local statute or regulation, or other State or local legal requirement, may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service.

(b) STATE REGULATORY AUTHORITY. - Nothing in this section shall affect the ability of a State to impose, on a competitively neutral basis and consistent with section 254, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers."

¹¹ Chairman Lynn Greer disagreed with the majority's position, stating:

As I see it, we have a direct conflict between a federal law and one of our state statutes, and federal law must prevail. I believe the federal Act obviously preempts our state statute Tenn. Code Ann. § 65-4-201(d), pursuant to the Supremacy Clause of Article VI of the United States Constitution. . . . I believe that upholding the Tennessee statute in this case would undermine competition and therefore contradict the goals of the

Tenn. Code Ann. § 65-4-201(d) is currently the law in the state of Tennessee as both parties have acknowledged. Recognizing this fact, I am not sitting as a policymaker on this piece of legislation. Whether I support the enactment of Section 65-4-201(d) is irrelevant. As noted by the court in Hamblen Cty Educ. Ass'n v. The Hamblen Cty Brd of Education, 892 S.W.2d 428, 432 (Tenn. App. 1994), "[i]t is not for the courts to question the wisdom of legislative enactments. We 'must take statutes as we find them.'" Therefore, as a Director of the TRA, it is not my place to question the wisdom of the general assembly.

Transcript of March 10, 1998, Directors' Conference, p. 9. Acting upon the Application, the majority then opined that the plain language of Section 253(a) of the Act appears to preempt Tenn. Code Ann. § 65-4-201(d). Still, as the FCC noted in the Texas Preemption Decision, if a challenged law or regulation satisfies the requirements of Section 253(b) of the Act, Section 253(a) does not act to preempt it. In other words, according to the FCC, Section 253(b) operates as a limitation upon any preemptive challenge launched by Section 253(a). Therefore, in the opinion of the majority, prior to concluding that § 65-4-201(d) is preempted by Section 253(a), it is imperative that the application of Section 253(b) be evaluated.

The Authority concluded that Tenn. Code Ann. § 65-4-201(d) is essential to preserving universal service within Tennessee, protects the public safety and welfare, ensures the continued quality of telecommunications services and safeguards the rights of consumers. The Authority so concluded on the basis that many of the small, independent local exchange companies and telephone cooperatives in Tennessee serve small areas with relatively few customers, and, typically, such small serving areas include a few large business customers whose revenues support the provision of affordable service to the companies' residential customers. If a competitor were

Telecommunications Act. . . . Obviously the Tennessee General Assembly felt very strongly about its position in this matter, and I have great respect for its opinion. However, I do believe that the federal statute is unambiguous and must prevail.

Transcript of March 10, 1998, Directors' Conference, pp. 7-8.

to begin serving the large business customers of the incumbent, a significant amount of universal service support could be lost, with residential and small business rates having to suffer an increase in order to make up for possible lost revenue. The Authority further concluded that such rate increases could jeopardize universal service within Tennessee.

Regarding the importance of preserving universal service, it is the position of the Authority that:

In the preamble to the Tennessee Telecommunications Act of 1995,¹² the Tennessee General Assembly stated that 'It is in the public interest of Tennessee consumers to permit competition in the telecommunications services market.' Further the Assembly stated that 'Universally affordable basic telephone service should be preserved.' Thus, the purpose of the Act is two-fold: to foster the development of competition, and to preserve universal service. Among other things, Section 65-4-201(d) ensures that for a period of time universal service is not disrupted while permanent universal service mechanisms are considered in the more rural areas of the state. The general assembly concluded that prematurely opening up the more rural areas of the state to competition without some transition period could result in untold consequences that may have substantial harmful effects on universal service in said areas.¹³

In order to ensure that rural consumers receive both the benefits of the development of an efficient technologically advanced statewide system of telecommunications and universal service during the introductory stages of competition in this previously monopolistic market, the General Assembly passed Section 65-4-201(d). Thus, Section 65-4-201(d) is, . . . as Section 253(b) requires, consistent with both state and federal universal service goals and objectives. In fact, . . . today, absent 65-4-201(d), the universal service objectives in Tennessee would not be advanced in rural areas and the goals of federal universal service may be irreparably undermined.

Transcript of March 10, 1998, Directors' Conference, pp. 10-11.

The requirement of competitive neutrality under Section 253(b) of the Federal Act was recognized as a more difficult inquiry. On that issue, the Authority found that Tenn. Code Ann. § 65-4-201(d) is competitively neutral because its restriction on entry into the service areas of

¹² 1995 Tenn. Pub. Acts 408.

¹³ Director Sara Kyle stated, for the record, her belief that the Tennessee legislature's policy was sound in promulgating Tenn. Code Ann. § 65-4-201(d).

small local exchange companies applies to all telecommunications service providers within the State. No provider is given a competitive advantage over any other in the areas served outside of the small local exchange companies' service territories. Also, Tenn. Code Ann. § 65-4-201(d) allows equal entry by all telecommunications service providers into the territories of a small local exchange company in the event that such small local exchange company seeks and is granted the authority to compete outside of its authorized service area.

Moreover, given the legislature's rationale for enacting § 65-4-201(d), the language of Section 253(b) as a whole, Section 65-4-201(d)'s pronouncement that any such protected incumbent forfeits its protection if it seeks to compete outside of its area, and the requirement that the general assembly review this statute every two years¹⁴, this statute may be held competitively neutral. In fact, with respect to all competitors, large or small, § 65-4-201(d) may be viewed as being unwaveringly competitively neutral.

If Section 253(b) is interpreted too narrowly, Section 253(b) may be read out of the statute, which is clearly not what Congress intended. To be sure, the Authority fully recognizes and respects the possibility that the FCC's application of Section 253(a) in circumstances similar to those presented in this matter may eventually become the law of the land. Conversely, however, it remains plausible that the FCC's interpretation, to the extent that it demands a different result than that adopted by the majority herein, may be in error. See cf., Iowa Utilities Board v. FCC, et al., 120 F.3d 753 (8th Cir. 1997) ("[W]e conclude that the Act plainly grants the state commissions, not the FCC, the authority to determine the rates involved in the implementation of the local competition provisions of the Act."). At this early stage of the development of the interpretation of Section 253(a), however, the Authority has determined that

¹⁴ See Tenn. Code Ann. § 65-5-211.

it would be premature to capitulate at this point, especially in light of the intent of the Tennessee General Assembly in enacting Tenn. Code Ann. § 65-4-201(d), and in protecting universal service in Tennessee. It may take some time for the FCC and perhaps the courts to hone the interpretation of Section 253 of the Act.

It is the opinion of the majority that Sections 253(a) and (b) of the Act must be read together, and when done so, there is little doubt that Congress intended that states retain the authority to preserve, protect, and promote universal service. Tenn. Code Ann. § 65-4-201(d) satisfies the requirements of Section 253(b) of the Act¹⁵ and, therefore, Section 253(b) operates as a limitation upon Hyperion's preemptive challenge under Section 253(a) of the Act.

For the foregoing reasons, the Authority denies Hyperion's application pursuant to Section 253(b) of the Act.

IT IS THEREFORE ORDERED THAT:

1. Hyperion's Application for a Certificate of Public Convenience and Necessity to extend its territorial area of operations to include the areas currently served by Tennessee Telephone Company is hereby denied;

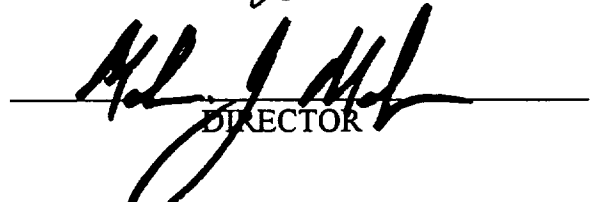
2. Any Party aggrieved by the Authority's decision in this matter may file a Petition for Reconsideration with the Authority within ten (10) days of the date of this Order; and

¹⁵ Codified as 47 U.S.C. § 253(b).

3. Any party aggrieved by the Authority's decision in this matter has the right of judicial review by filing a Petition For Review in the Tennessee Court of Appeals, Middle District, within sixty (60) days of the date of this Order.


CHAIRMAN


DIRECTOR


DIRECTOR

ATTEST:


EXECUTIVE SECRETARY



Tennessee Regulatory Authority, Authorization No. 316236, 500 copies, March, 1999. This public document was promulgated at a cost of \$15.29 per copy.